Supreme Court, U.S.
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No. 02-

IN THE
Supreme Court of the United States

FUTURESOURCE, LLC,

Petitioner,

v.

REUTERS LIMITED; REUTERS SA;
and REUTERS AMERICA, INC.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. May a bankruptcy "free and clear" sale of a debtor's property under 11 U.S.C. § 363(f) be used to defeat the special protections that 11 U.S.C. § 365 provides for parties to certain types of executory contracts with the debtor, including specifically lessees of real property (§ 365(h)) and licensees of intellectual property (§ 365(n)).

2. Do the bankruptcy protections that 11 U.S.C. § 365(n) provides to licensees of intellectual property under executory contracts with the debtor-licensor encompass the licensee's rights to post-petition modifications of the intellectual property independently made by the licensor.

RULE 29.6 CORPORATE DISCLOSURE STATEMENT

FutureSource LLC has no parent corporations and no publicly held company owns 10% or more of its stock.

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Petitioner FutureSource, LLC, respectfully petitions this Court for a writ of certiorari to review the judgment of the United States Court of Appeals for the Seventh Circuit in this case.

OPINIONS BELOW

The opinion of the Seventh Circuit is reported at 312 F.3d 821. The opinion is reproduced in the Appendix at 1a-9a. The opinions and orders of the United States District Court for the Northern District of Illinois, dated March 29, 2002, April 5, 2002, April 15, 2002 and April 25, 2002 are not reported; they are reproduced at 10a-27a.

STATEMENT OF JURISDICTION

The judgment of the Seventh Circuit was entered on November 27, 2002. 1a. The jurisdiction of the Seventh Circuit was based on 28 U.S.C. § 1292(a)(1). The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

The relevant portions of 11 U.S.C. §§ 363 and 365 are attached at 28a-33a.

STATEMENT OF THE CASE

Facts. Petitioner FutureSource Information Systems, Inc., now FutureSource LLC ("FutureSource"), and Bridge Information Systems Inc. ("Bridge") formed FutureSource/ Bridge LLC to conduct market information and analysis software businesses in the commodities field. L2[1]. As part

1. "a" refers to the short appendix attached to this Petition. "L" refers to FutureSource's separate lodging filed herewith.

of the formation of FutureSource/Bridge LLC, FutureSource entered a contract with Bridge, the "Intercompany Services Agreement" ("ISA"), under which, in exchange for initial capital and ongoing royalties of approximately $1.5 million a year, Bridge licensed to furnish FutureSource with continuously updated and reformatted financial market data for resale to FutureSource's customers. The information product is supplied via proprietary software necessary to manipulate and deliver the data.

The intellectual property encompassed by the licenses includes three products known as Bridge Station, Bridge Channel and Bridge Feed (collectively referred to as the "Bridge Products"). L16. These are computer software programs, including embedded streaming data. The licenses in the ISA give FutureSource the rights to receive, use and sell access to the Bridge Products in their continuously updated form. L16-34.

The licenses obligate the intellectual property owner (initially, Bridge) to provide FutureSource and its customers with access to the Bridge Products as long as the owner provides those products to its own customers. L23. In the ISA, Bridge granted FutureSource an exclusive license to sell Bridge Station and Bridge Feed in North America and Europe (except France) to certain end users, like futures commissions merchants, and also to certain specific companies, and a nonexclusive license to sell elsewhere. L16, 20. The license for Bridge Channel was worldwide and not exclusive. L21.

Two years after entering the ISA, Bridge filed for bankruptcy. 2a. Bridge identified the ISA as an executory contract. L5. The Bridge debtors continued to operate and manage their businesses as debtors in possession. L4.

The bankruptcy court conducted an auction to sell Bridge's assets under 11 U.S.C. § 363. Pursuant to an asset purchase agreement ("APA"), Respondent Reuters contracted to buy for $275 million substantially all of the assets used in Bridge's financial-market data services, including, as a small portion of such assets, the Bridge Products licensed to FutureSource. 2a. The APA provided that the "Purchaser [Reuters] shall assume from sellers [Bridge] . . . all (i) . . . obligations and liabilities with respect to, arising out of, or associated with the ownership, possession or use of the Acquired Assets [including the Bridge Products] . . . arising on or after the Closing Date." 2a; R. 8, Ex. B, p. 7 (§ 2.6).

In its order ("Sale Order") approving the asset sale to Reuters, the bankruptcy court indicated that the assets Reuters was purchasing included the Business Assets which included the Bridge Products (L61), and stated that Reuters was taking the assets free and clear of all "liens, claims, interests, and encumbrances." L58. The Sale Order also identified certain of Bridge's executory contracts that would be assumed by the trustee and purchased by Reuters (which did not include the ISA) (L60). The Sale Order also gave Reuters the right to have assumed and assigned to it other executory contracts whose identity was kept secret by Reuters and Bridge. L48, 54; R8, Ex. B, p. 6. Beyond this, the Sale Order excluded Bridge's executory contracts from its scope (L49), and contemplated later §§ 363/365 sales of executory contracts (L60).

FutureSource was not a party to the bankruptcy proceeding. 3a. FutureSource put its name on the general service list, and it received notice of the Reuters-Bridge asset purchase and sale. 3a. FutureSource did not object to the sale or challenge the Sale Order. Except as stated above — *i.e.*, that certain identified executory contracts would be

assumed and assigned to Reuters, and that Reuters had similar rights with respect to other, unidentified executory contracts — neither the notice nor the Sale Order indicated that the Reuters-Bridge asset purchase and sale was intended to or would affect any rights under Bridge's executory contracts (including specifically FutureSource's license rights in the Bridge Products under the ISA).

Reuters did not purchase the license rights in the ISA in the bankruptcy proceeding. However, the trustee did assume that contract, and sold and assigned it to another company, Moneyline Network. 3a. That occurred before Reuters completed its asset purchase of the Bridge Products. L76. Reuters had notice of these events and made no objection. L5.

During the bankruptcy proceeding, Bridge and Reuters respectively performed the obligations owed to FutureSource under the ISA. R. 33, Ex. 6, p. 2. However, a dispute arose between FutureSource and Reuters concerning FutureSource's licenses. L6. Reuters claimed that through its purchase of the debtor's assets, it was acquiring the Bridge Products free and clear of FutureSource's rights under the licenses; and it threatened to cut off FutureSource's access to the Bridge Products after the purchase transaction closed. L6. FutureSource contended that Reuter's purchase of the intellectual property constituting the Bridge Products was subject to FutureSource's license rights under the ISA. L6.

To provide the parties with time to work out an arrangement concerning the licenses, Reuters and FutureSource entered into a temporary FutureSource/Bridge Services Agreement (the "Interim Agreement"). L7, 35-47. As the end of the Interim Agreement approached, Reuters contacted and solicited FutureSource's customers, telling

them that FutureSource would no longer have a license to sell, market or distribute the Bridge Products and they would no longer be able to receive the Bridge Products from FutureSource. L8. FutureSource brought this suit to compel Reuters to continue providing access to the Bridge Products that Reuters is providing to its own customers. L1-15[2].

Proceedings Below. FutureSource filed a complaint in the federal district court based on diversity of citizenship. FutureSource alleged claims for tortious interference with contract, tortious interference with prospective economic relations, and breach of contract, and sought a temporary restraining order and preliminary injunction requiring Reuters to continue to provide FutureSource access to the Bridge Products. L1-15.

The district court granted a temporary restraining order, finding that FutureSource was likely to succeed on the merits, that it had a license to receive and sell the Bridge Products, that Reuters was obligated to provide the Bridge Products to FutureSource and its customers, and that 11 U.S.C. § 365(a) applied because the executory contract was not rejected but rather assumed and assigned in the bankruptcy. 20a-27a. The district court subsequently converted the temporary restraining order into a preliminary injunction, finding that because the licenses granted rights in intellectual property

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2. As with Bridge before it, Reuters contracts with various financial exchanges to obtain the continuously updated trade secret data part of the intellectual property encompassed by the licenses. Reuters then reformulates the data using proprietary software to create the Bridge Products. L20-26. Reuters produces the Bridge Products for its own purposes, independent of FutureSource's rights under the licenses. Reuters itself sells the Bridge Products to retail customers. It also uses the Bridge Feed in its competing products and licenses it to other resellers. R8, Ex. B, p.1.

owned by the debtor, Reuters purchased that intellectual property subject to those license rights. 14a-19a. The district court ruled that the bankruptcy court's "free and clear" order did not affect the Bridge Product licenses. *Id.*

Reuters appealed the preliminary injunction, and the Seventh Circuit reversed. Writing for the Court, Judge Posner concluded, contrary to the district court, that the bankruptcy court's § 363(f) "free and clear" sale extinguished all "interests" in the assets acquired, including FutureSource's license rights in the intellectual property constituting the Bridge Products. 5a-6a. Judge Posner reasoned that FutureSource consented to the sale of the Bridge assets, including the intellectual property to which it had license rights, because it had notice of and did not object to the § 363 asset sale. 3a. He alternatively concluded that because Moneyline rather than Reuters purchased Bridge's rights in the ISA, FutureSource had no contract rights against Reuters in the updated data after the Bridge assets were purchased by Reuters. 7a-9a.

REASONS FOR GRANTING THE PETITION

I. The Decision Below Erroneously Nullifies the Bankruptcy Protections That 11 U.S.C. § 365 Provides to Licensees of Intellectual Property and Lessees of Real Property.

The decision below rules that an asset sale under 11 U.S.C. § 363(f) may be used to defeat the special protections that 11 U.S.C. § 365 provides to parties to certain types of executory contracts with the debtor. That effectively reads §§ 365(h) and (n) out of the Bankruptcy Code. The decision stands virtually alone against a broad and long-established body of bankr ptcy and intellectual property

law. It nullifies the crucial protections for licensees of intellectual property, and for the entire system of intellectual property licensing, that Congress intended to protect by enacting § 365(n) in the Intellectual Property Bankruptcy Protection Act of 1988. The Court should grant review to clarify that § 365 meaningfully protects the rights of lessees of real property and licensees of intellectual property owned by bankruptcy debtors.

A. Under 11 U.S.C. § 365, A Bankruptcy Proceeding May Not Be Used To Strip Intellectual Property Licensees and Real Property Lessees of Their Rights In the Subject Property.

Under the Bankruptcy Code, contracts are executory where some material performance or obligation is still owing by both parties. *E.g.*, *NLRB v. Bildisco & Bildisco*, 465 U.S. 513, 522 n.6 (1984). These contracts are dealt with under 11 U.S.C. § 365, which generally gives bankruptcy trustees and debtors in possession broad authority either to assume or to reject executory contracts. If the contract is assumed, the trustee (or debtor) must cure any prior defaults and provide assurance that it will fully perform the contract in the future. § 365(b)(1). After an executory contract is assumed, the debtor's interest in the contract (both rights and obligations) is frequently sold and assigned to a third party. Section 365 contemplates these assignments, and the other party to the executory contract generally cannot prevent the assignment as long as there is adequate assurance the assignee (purchaser) will perform. 11 U.S.C. § 365(f)(2)(B).

On the other hand, if the trustee (or debtor) rejects an executory contract, this ordinarily terminates the contract and the other contracting party is made a general creditor for losses caused by the debtor's breach. 11 U.S.C. § 365(g).

However, certain types of executory contracts are treated differently under § 365. In particular, special protections are provided for lessees of real property owned by the debtor, 11 U.S.C. § 365(h), and for licensees of intellectual property owned by the debtor, 11 U.S.C. § 365(n).[3]

When an executory lease of real property owned by the debtor is rejected, the lessee may elect to retain its possessory rights for the remaining term of the lease subject to payment of ongoing rent (with a right of set off for debtor's non-performance of ongoing obligations after the date of rejection). 11 U.S.C. §§ 365(h)(1)(A) and (B); *see, e.g., In Re Flagstaff Realty Associates*, 60 F.3d 1031, 1033-34 (3rd Cir. 1995). Licensees of intellectual property owned by the debtor are treated in a similar fashion under § 365(n). If the debtor rejects an executory license, the licensee may elect to retain its rights in the intellectual property (including a right to enforce any exclusivity provision) for the remaining term of the license, subject to payment of ongoing royalties. 11 U.S.C. §§ 365(n)(1)(B) and (2); *see, e.g., In Re Prize Frize, Inc.*, 32 F.3d 426, 428 (9th Cir. 1994).

Congress enacted § 365(n) as part of the Intellectual Property Bankruptcy Protection Act of 1988. That legislation was in reaction to certain court decisions, which had held that a bankruptcy debtor's rejection of an executory contract resulted in forfeiture of all of the licensee's rights in the subject intellectual property. The most notorious of these decisions, *Lubrizol Enterprises, Inc. v. Richmond Metal Finishers, Inc.*, 756 F.2d 1043 (4th Cir. 1985), is extensively

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3. The Code also provides special protections for purchasers under executory contracts selling real property of the debtor. 11 U.S.C. § 365(i).

discussed in the legislative history. S. Rep. 100-505, at 2, 11-13 (1988), *reprinted in* 1988 U.S.C.C.A.N. 3200, 3201, 3209-10, attached at 34a-55a. Under that interpretation of § 365, the trustee/debtor could unilaterally strip license rights from intellectual property where that would permit the property to be sold in bankruptcy for a higher price. 756 F.2d at 1047-48. The legislative history noted that such stripping of the licensee's rights "will nearly always be beneficial to the bankruptcy estate," but it imposed too heavy a "burden on American technological development. . . ." S. Rep. 100-505, at 3; 36a.

> This view [that a § 365 rejection can strip intellectual property license rights] . . . leaves licensees in a precarious position and thus threaten[s] the very flexible and beneficial system of intellectual property licensing that has developed in the United States. . . .
>
> The court decisions on Section 365 that have stripped intellectual property licensees of their right to continue to use the licensed property . . . threaten an end to the system of licensing of intellectual property (discussed below) that has evolved over many years to the mutual benefit of both the licensor and the licensee and to the country's indirect benefit . . . This change . . . is wasteful and cumbersome and is especially chilling to small business technologists. *It is not an overstatement to say that the change is a fundamental threat to the creative process that has nurtured innovation in the United States.*

S. Rep. 100-505, at 3-4; 36a-37a (emphasis added); *see also, e.g.*, Marjorie F. Chertok, *Structuring License Agreements*

With Companies in Financial Difficulty: Section 365(n) — Divining Rod or Obstacle Course?, 65 St. John's L. Rev. 1045, 1053-56 (1991) (discussing background of legislation adding § 365(n)).

Significantly, Congress specifically modeled its protection for intellectual property licensees under § 365(n) on the special provisions for real property lessees under § 365(h):

> The bill provides for treatment of intellectual property licenses under Section 365 in a manner that parallels generally the treatment of real estate leases in the existing provisions of Section 365(h)(1). While intellectual property plays a unique role in technological and economic development, the problems associated with rejection of executory contracts are common with other special forms of property, such as real property leases. In both real estate leases and intellectual property licenses, the underlying property is unique.

S. Rep. 100-505, at 6; 39a.

B. Section 365's Protections May Not Be Evaded By A So-Called "Free and Clear" Sale of the Debtor's Property Under § 363(f).

Even though § 365(n) was enacted specifically to prevent debtors from increasing the value of the bankruptcy estate by stripping license rights from intellectual property, the decision below holds that § 363(f) permits the debtor to

accomplish that same result through an asset sale of the intellectual property. The Seventh Circuit held that:

> The Bankruptcy Court's sale order, consistent with 11 U.S.C. § 363(f), extinguished all 'interests' in the assets acquired . . . and this included any interest in the intellectual property.

5a-6a.

This holding squarely presents the issue whether a § 363(f) asset sale may be used to evade the special protections Congress provided for intellectual property licenses under § 365(n). The significance of the Seventh Circuit's decision, however, is even broader. Given Judge Posner's reasoning using leaseholds as the analogy, with citations to cases deciding the exact issue under § 365(h),[4] the decision below effectively holds that § 363(f) asset sales may also be used to evade § 365 protections for real property lessees.

As the Seventh Circuit's discussion implies, previous litigation concerning the interplay between asset sales under § 363(f) and special protections for certain executory contract holders under § 365 has involved § 365(h) and its protection of rights of real property lessees. With one exception, courts have held that asset sales under § 363(f) *do not* defeat the lessee's 365(h) rights to continue the leasehold if the lease is rejected. *Precision Indus., Inc. v. Qualitech Steel SBQ, LLC*, No. IP 00-247-C H/G, 2001 U.S. Dist. LEXIS 8328,

4. "Although the statute does not define 'interest,' leaseholds are an interest, e.g., *In re Downtown Athletic Club*, No. M-47 (JSM), 2000 WL 744126, at *4 (S.D.N.Y. 2000); *In re Taylor*, 198 B.R. 142, 161-62 (Bankr. D.S.C. 1996), and leaseholds are FutureSource's own chosen analogy to Bridge's license." 6a.

at *27-46 (S.D. Ind. April 24, 2001), *aff'd*, 276 F.2d 245 (7th Cir. 2001); *In re Taylor*, 198 B.R. 142, 164-67 (Bankr. D.S.C. 1996); *In re Churchill Properties III, LP*, 197 B.R. 283, 286-88 (Bankr. N.D. Ill. 1996). *See also* 3 Collier on Bankruptcy ¶ 365.10[1] (15th Ed. Rev. 2003); *In Re Independence Village, Inc.*, 52 B.R. 715, 732-33 (Bankr. E.D. Mich. 1985) (life care residents' lease rights under § 365(h) could not be circumvented by § 363(f) sale); *In Re LHD Realty Corp.*, 20 B.R. 717, 719 (Bankr. S.D. Ind. 1982) (§ 365(h) "is the exclusive remedy available to a debtor in an executory lease situation"). One decision, cited by the Seventh Circuit, is to the contrary but contains no analysis and merely asserts its conclusion. *In Re Downtown Athletic Club*, No. M-47 (JSM), 2000 WL 744126, at *4 (S.D.N.Y. June 9, 2000).[5]

The courts analyzing this issue have relied on basic tenets of statutory construction to conclude that § 365's protections for executory contracts control § 363's sales provisions. First, the more specific protections of § 365 as to particular types of property control over the general sale provisions of § 363. *E.g.*, *In Re Churchill Properties*, 197 Bankr. at 288. This is a paradigm application of a canon of construction that this Court frequently employs. *E.g.*, *Morales v. Trans World Airlines, Inc.*, 504 U.S. 374, 385 (1992) (Congress would not intend a carefully drawn, substantive provision to be rendered null by general "savings" provision).

Second, Congress' intent under § 365(h) was to prevent the "lessee's interest in a leasehold [from being] . . . modified

5. The Seventh Circuit also cites *In re Taylor*, but fails to note that *Taylor* is a leading authority holding that a § 363(f) asset sale *does not* defeat lessees' rights protected by § 365(h). 6a. 198 B.R. at 164-67. Although the Seventh Circuit opinion declines to cite § 365(n) specifically, FutureSource placed principal reliance on that statute in both the district court and the Seventh Circuit. Dck. Nos. 2, 10, 33; FutureSource Response Br. pp. 28-35.

or changed because of a pending bankruptcy," whereas allowing a sale under § 363 to override § 365(h) would render the latter provision "nugatory." *In Re Churchill Properties*, 197 B.R. at 288. This reasoning follows the rule of construction that statutes should be read to give effect, where possible, to all their parts. *See, e.g., FCC v. Nextwave Personal Communications, Inc.*, 123 S. Ct. 832, 839 (2003) (a reading of Bankruptcy Code § 525(a) that makes its exceptions superfluous "must be rejected"); *Kawaauhau v. Geigle*, 523 U.S. 57, 61-62 (1998) (rejecting interpretation of Bankruptcy Code § 523(a)(6) that obviates the need for § 523(a)(9)); *see also In Re National Gypsum Co.*, 208 F.3d 498, 507 (5th Cir. 2000) (Bankruptcy Code § 1141(d) may not be read in a manner that would nullify cure requirement of § 365(b)(1)).

The same reasoning applies to § 365(n) with equal or greater force. In enacting that statutory amendment, Congress specifically determined that:

> The [intellectual property] licensee requires retention of its rights, even exclusive rights. *No longer can the debtor expect to sell these rights through rejection.*

S. Rep. 100-505, at 15; 48a. Under the Seventh Circuit's decision, however, the debtor is allowed to "sell these rights" through a § 363(f) sale. That result mocks Congress' determination that the intellectual property licensee "requires retention of its rights." Henceforth, debtors will use this device whenever the intellectual property is determined to be of greater value to the bankruptcy estate if free of the licensee's rights. That is, of course, every case in which

§ 365(n)'s special protections are needed.[6] The result makes § 365(n) meaningless as a practical matter.

As the legislative history of § 365(n) sharply illustrates, this is a critical issue for the continued dependability and flexibility of the Nation's intellectual property licensing system. Congress enacted § 365(n) to guard against the very result reached below, which permits debtors to increase the value of estate property by stripping the rights of intellectual property licensees. Congress determined that statutory protection against that result was necessary "to restore confidence in the system of intellectual property licensing. . . ." S. Rep. 100-505, at 13; 46a. The decision below now reintroduces "the obvious disincentive to the full development of intellectual property" that Congress intended to abolish. *Id.*

Moreover, the Seventh Circuit's decision is likely to have an even broader impact because of its reliance upon the leasehold analogy and authorities decided under § 365(h). "Free and clear" asset sales under § 363 will also be used to strip real property lessees of leasehold rights intended to be protected by § 365(h), just as was permitted by the aberrant *Downtown Athletic Club* decision the Seventh Circuit's opinion relies upon.

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6. Congress recognized this in passing § 365(n), noting that the cases "nearly always" resulted in rejection of intellectual property licenses "since rejection results in valuable rights apparently reverting to the bankruptcy estate — rights the bankruptcy estate otherwise would have to share with the licensee." S. Rep. 100-505, at 3; 36a.

C. The Seventh Circuit's "Consent to Sale" and "Collateral Attack" Theories Are Circular and Erroneously Assume a § 363(f) Sale Results in Loss of Licensee and Lessee § 365 Rights in the Subject Property.

The decision below reasons that the FutureSource "consented" to the sale of the subject intellectual property "free and clear" of its license rights because it had notice of the § 363 asset sale and did not object. The opinion also suggests that because the § 363(f) sale extinguished its license rights, FutureSource's action to enforce its rights is an improper collateral attack on the bankruptcy court's Sale Order. 6a-7a. This reasoning is simply a less direct path to the result that § 363(f) asset sales override §§ 365(h) and (n) rights. Notice of a § 363(f) asset sale and failure to object could constitute "consent" *to loss of intellectual property license rights* (or of real property leasehold rights) only *if that were the legal consequence* of a § 363(f) sale. The "consent" and "collateral attack" theories thus assume the answer to the real question — they assume that a § 363(f) sale has these § 365 rights-stripping consequences.

Purchasers of assets from § 363(f) sales often claim that a previous "free and clear" sale and order had the effect of wiping out various types of rights. Courts have properly rejected these asset-purchaser contentions. The Seventh Circuit's "consent" and "collateral attack" theories are refuted by these authorities

For example, *after* § 363(f) "free and clear" asset sales, courts have rejected purchaser contentions that the bankruptcy court order and sale had the effect of stripping lessees of § 365(h) rights to continue their leaseholds.

Precision Industries, 2001 U.S. Dist. LEXIS 8328, *57-67.[7]; *In Re Churchill Properties*, 197 B.R. at 286-88. Similarly, *In Re Wolverine Radio Co.*, 930 F.2d 1132, 1145-49 (6th Cir. 1991), rejected the asset purchaser's contention that a previous § 363(f) asset sale had the effect of wiping out the debtor's unemployment compensation experience rating relating to those assets. *Folger Adams Security Inc. v. Dematteis/MacGregor, JV*, 209 F.3d 252, 265 (3d Cir. 2000), held that a previous § 363(f) "free and clear" sale did not wipe out affirmative defenses or recoupment rights relating to a purchased asset (an account receivable). *Accord In Re Lawrence*, 221 B.R. 661, 670 (Bankr. N.D. N.Y. 1998). Similarly, a § 363 notice and sale of real property does not wipe out easement rights. *In Re Oyster Bay Cove, Ltd.*, 196 B.R. 251, 255-56 (Bankr. E.D. N.Y. 1996) ("free and clear" refers to interests such as liens and mortgages which attach to the proceeds of the sale, not easement rights).

In *Folger*, the Third Circuit also concluded that a § 363 free and clear sale notice did not give the person allegedly indebted on the account receivable notice that the sale would wipe out its recoupment rights, because a § 363 sale does not affect such rights and the notice did not specify otherwise. 209 F.3d at 265. *Folger* found that a contrary ruling would violate due process rights — if a § 363(f) "free and clear" sale is intended to have unusual effects as to particular assets, the notice must specifically so state. *Id.* Similar concerns were voiced in *In Re National Gypsum Co.*, 208 F.3d 498,

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7. The court in *Precision Industries* correctly observed that the asset purchaser's "interpretation of the Sale Order" was based upon that party's "preferred view of the relationship between Section 363 and Section 365" — that is, it "assumed that a sale under Section 363(f) can terminate all unassumed leases of a debtor-leasor." 2001 U.S. Dist. LEXIS 8328, at *59.

510-512 (debtor must give *specific* notice to executory contract holders in order to affect their rights). *See also, e.g., In Re Savage Indus., Inc.*, 43 F.3d 714, 720-23 (1st Cir. 1994) (even assuming a § 363(f) asset sale could have the legal effect of shielding asset purchaser from successor liability claims, the previous sale at issue could not have had such an effect without specific notice to the tort claimants). The same analysis applies here. The § 363 sale could not override FutureSource's § 365(n) rights and the sale notice did not purport to say otherwise.[8]

This "consent" aspect of the Seventh Circuit's decision also will disrupt the administrative process of § 363 sales. It will create congestion and confusion in the bankruptcy courts by forcing lessees and licensees to appear and object to § 363 sales even though they do not know and cannot determine whether their § 365 rights will be (or will later be claimed to be) affected by the sale.

A hypothetical illustrates the point. Mr. Smith owns a personal computer and buys and installs Windows XP™ as his operating software (as tens of millions of us have done). He has an executory license for the software (intellectual property)[9] and is entitled to upgrades and routine maintenance

8. Indeed, under the terms of the APA, Reuters was to take the purchased assets subject to their attendant obligations, and Reuters and the debtor kept secret the identity of the contracts Reuters would later cause to be assumed and purchased. *See*, p. 3, *supra*.

9. Under such a license, the license holder may typically only use the software for personal home or business use, may not copy it, and may not exploit it for commercial purposes. *See, e.g., ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447, 1450 (7th Cir. 1996) (Easterbrook, J.) (software shrinkwrap license enforceable to prevent licensee from commercial use per its terms).

for his software to the extent the software owner provides them. The Government sues Microsoft for antitrust violations, wins, and Microsoft goes bankrupt. The trustee sells Microsoft's intellectual property assets including Windows XP™ to Company X in a § 363(f) "free and clear" sale. Mr. Smith is given no specific notice concerning § 365(n) rights. He may or may not have seen a general notice in the newspaper that Windows XP™ is being sold. He does not object (and neither do the other 100 million license holders). Under the Seventh Circuit's decision, Company X can tell Mr. Smith that he cannot continue to use Windows XP™. His license rights have been erased by the § 363 "free and clear" asset sale.

Thus, thousands of real property lessees and intellectual property license holders in large national bankruptcies, such as WorldCom, K-Mart, United Airlines and Enron will need to appear and object to § 363(f) sales to protect themselves under the Seventh Circuit's "consent" theory. The Fifth Circuit warned of a similar scenario in *In Re National Gypsum Co.*:

> Adoption of [the Debtors'] contrary analysis would have a perverse effect outside the scope of this case, an effect that would be felt by non-debtor parties whose contracts or leases are rejected. Contrary to the explicit statements of the Code, the act of rejection would only create a bona fide claim for damages if the non-debtor had already filed a preemptive, conjectural proof of claim . . . This scheme — unappealing from a policy perspective as it would result in a deluge of potentially pointless preemptive proofs of claim — is inconsistent with [the Bankruptcy Code].

208 F.3d at 505 n.6.

D. The Supposed Absurd Consequences In This Case Result From Reuters' Actions and Provide No Basis For Rewriting The Statutory Scheme.

As discussed, § 363 does not defeat the protections of § 365(n). The trustee, therefore, took the intellectual property as he found it and sold it without affecting the outstanding licenses. *Bildisco*, 465 U.S. 513, 531 (debtor who assumes contract assumes it *cum onere*). Bankruptcy law, therefore, does not apply. The respective rights of the purchaser of the intellectual property and the licensee are determined according to the non-bankruptcy law that governs intellectual property.

Courts addressing the issue under non-bankruptcy law have uniformly held that a purchaser of intellectual property with notice takes subject to existing third party license rights in that property. *E.g.*, *Waterman v. Mackenzie*, 138 U.S. 252, 258 (1891) (federal law makes patent assignments subject to the conditions of any licenses previously conferred by the patent holder); *New York Phonograph Co. v. Edison*, 136 F. 600, 605 (C.C. S.D.N.Y. 1905), *aff'd*, 144 F. 404 (2d Cir. 1906) (Thomas Edison was held to have re-purchased his own patent subject to intervening third party rights, including license rights); *L. L. Brown Paper Co. v. Hydroiloid, Inc.*, 118 F.2d 674, 677 (2d Cir. 1941) (purchaser through receiver took patents subject to existing licenses); *Kenyon v. Automatic Instrument Co.*, 160 F.2d 878, 884 (6th Cir. 1947) (purchaser in receivership "free and clear" sale did not take the intellectual property free of, but rather subject to, outstanding license rights); *In Re Access Beyond Technologies, Inc.*, 237 B.R. 32, 38 (Bankr. Del. 1999); *In Re Novon Int'l*, Nos. 98-CV-677 E(F), 96-BK-15463B, 2000 U.S. Dist. LEXIS 5169, 2000 WL 432848 (Bankr. W.D. N.Y. March 31, 2000) (§ 363 purchaser of intellectual property took subject to outstanding license rights). The Seventh Circuit has also recognized this rule. *In Re FedPak Systems*, 80 F.3d 207, 210 n.4 (7th Cir. 1996).

The Seventh Circuit suggests that application of this traditional legal rule would yield an absurd result — so much so, according to the Court, that allowing it would be "a serious indictment of American law" — because FutureSource would have license rights in the intellectual property but Reuters would not be entitled to the corresponding royalties. 5a-6a. However, the fact Reuters purchased intellectual property subject to outstanding licenses without taking the contractual benefits attendant to those licenses is a situation created by the trustee and Reuters, not FutureSource.[10] That is no basis for stripping FutureSource of its license rights, much less for distorting the bankruptcy statutes and reinstituting the threat to the intellectual property licensing system that Congress so clearly meant to abolish.[11]

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10. Reuters could have had the trustee assume the ISA under § 365 and assign it to Reuters, in which case Reuters and FutureSource would each have had all of the contractual benefits and obligations (including, obviously, FutureSource paying Reuters the royalty). Alternatively, Reuters could have required the trustee to reject the ISA under § 365, in which case Reuters would have been entitled to the royalty payments under § 365(n)(2)(B). The only thing Reuters could *not* do if it wanted the royalties is what it did — allow the trustee to assume the contract and assign it to another purchaser. *In Re Novon*, 2000 WL 432848 at *5-7, 10-11. FutureSource had absolutely no control over which of the alternatives Reuters chose, and it bears no legal responsibility for the consequences of Reuters' choice. If Reuters is entitled to legal relief from the situation into which it placed itself, it must seek that remedy from Moneyline and/or the bankruptcy estate. FutureSource is indifferent as to who receives the royalty payments. But Reuters is not entitled to extricate itself from its self-selected predicament by stripping FutureSource of its license rights.

11. Contrary to the Seventh Circuit's implication, there is no necessary absurdity in splitting entitlement to the royalty stream from

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The legally significant anomalies arise from the Seventh Circuit's decision, which strips FutureSource of its license rights, including exclusive rights to particular products, customers and geographic areas, without notice, without compensation, without observing § 365(n)'s protections, and without honoring Congress' express intent in enacting that statute. Other anomalies under the Bankruptcy Code abound. First, under § 365, executory contracts may only be assumed *cum onere*. *Bildisco*, 465 U.S. at 531. The ISA was assumed in the bankruptcy proceeding, but under the Seventh Circuit's decision *cum onere* assumption is impossible, because the § 363 asset sale makes the executory contracts' most important provisions incapable of performance. Second, "[u]nless and until the trustee rejects" a contract licensing intellectual property, "the trustee *shall*" perform the contract or provide the intellectual property to the licensee and "*shall not*" interfere with the licensee's rights to such intellectual property. 11 U.S.C. § 365(n)(4)(A) (emphasis added). Under the Seventh Circuit's decision, this mandatory duty of the trustee is rendered impossible of performance after a § 363(f) sale of the intellectual property.

Third, under § 363(e), when an estate asset is sold free and clear of an "interest" in the property, that "interest" is to attach the sale proceeds (or to other security). *See, e.g.*,

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(Cont'd)

ownership of the intellectual property. The parties to intellectual property transactions may wish to accomplish that result for a variety of reasons and American law is sufficiently sophisticated to accommodate them — as patiently explained in the on-point authority the Seventh Circuit derides the district court for relying upon. *See In Re Novon*, 2000 WL 432848 at *5 (discussing, *inter alia*, *Walker on Patents*, § 20:47).

George W. Kuney, *Misinterpreting Bankruptcy Code § 363(f) and Undermining the Chapter 11 Process*, 76 Am. Bankr. L.J. 235, 237 n.46 (2002). No security was provided for FutureSource's licenses that were stripped from the intellectual property under the Seventh Circuit's decision. These manifest distortions of the § 363 and § 365 processes also show that review of the decision below is warranted.

II. The Seventh Circuit's Alternative Holding Erroneously Nullifies § 365(n)'s Protections For Large Categories Of Intellectual Property.

The decision below alternatively rules that FutureSource has no meaningful rights to the licensed intellectual property, because it would be entitled only to "stale" data it previously received from Bridge. Judge Posner reasons that, after the § 363(f) asset sale, Reuters generates the "future data," whereas FutureSource's contract right to future data supposedly runs only against Moneyline (because the debtor assumed the ISA and assigned it to Moneyline). 8a. FutureSource's "position" is said to "fail to distinguish between property that does and property that does not exist," and the bottom line is that FutureSource "has no license in data that Bridge-Reuters has not yet created." 7a, 8a.

This reasoning is not correct if considered in terms of substantive intellectual property law, which has long recognized rights in intellectual property to be created in the future. *E.g.*, *Littlefield v. Perry*, 88 U.S. (21 Wall.) 205, 226 (1874) ("An assignment of an imperfect invention, with all improvements upon it that the inventor may make, is equivalent in equity to an assignment of the perfected results"); *L.L. Brown Paper Co.*, 118 F.2d 674, 675 (patent license included future patent applications and future patents issued on the applications); *Aspinwall Mfg. Co. v. Gill*, 32

F. 697, 699 (C.C.N.J. 1887) (Bradley, Circuit Justice) (assignment of patent "[t]ogether with all improvements I hereafter make").[12]

This traditional view of the scope of protectible intellectual property is controlling in the bankruptcy context presented here. The statutory amendment adding § 365(n) encompasses intellectual property "whether protected by federal or state law, statutory or common law"; and it "in no way . . . alters any substantive intellectual property law [but rather] . . . refers to those rights which are already protected by applicable non-bankruptcy law." S. Rep. No. 100-505, at 7-8; 42a; *see also* 11 U.S.C. § 101(35A) (bankruptcy definition of "intellectual property" enacted by the same legislation).

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12. As Justice Bradley explained in *Aspinwall Manufacturing*:

> [W]here a man purchases a particular machine secured by a patent, and open to an indefinite line of improvements, it is often of great consequence to him that he should have the benefit of any future improvements that may be made to it. Without that, the whole value of the thing may be taken away from him the next day.

32 F. at 700. *See also, e.g., Conway v. White*, 9 F.2d 863, 866 (2d Cir. 1925) ("if a vendor sells future acquisitions — in this case musical compositions at the time unwritten — the equitable title attaches to the property the moment it comes into existence and vests in the grantee") (citation omitted); *Reece Folding Mach. Co. v. Fenwick*, 140 F. 287, 288 (1st Cir. 1905) (contracts "covering inventions to be afterwards made . . . are essential to the business of the contracting parties, and are not unjust"); *Westinghouse Air-Brake Co. v. Chicago Brake & Mfg. Co.*, 85 F. 786, 791 (C.C.N.D. Ill. 1898) ("An assignment of an imperfect invention, with all improvements upon it that the inventor shall make, is equivalent in equity to an assignment of the perfected results").

The Seventh Circuit's alternative holding thus presents the issue whether § 365(n)'s protections include a licensee's rights to future improvements and other changes to the intellectual property made by the debtor/licensor (and any subsequent assignee). To return to the Microsoft Windows XP™ example, the question is whether, if the executory contracts are rejected, § 365(n) protects licensee rights to receive software upgrades that the licensor independently makes and distributes. Where the debtor/trustee *assumes* the executory contract containing the license agreement (as happened here), a § 363(f) sale of the subject intellectual property should not deprive the licensee of rights it could unilaterally choose to retain under § 365(n) if the contract were *rejected*.[13] Those rights, specified in §§ 365(n)(1)(B), 2(A) and (3), run against any purchaser/assignee of the intellectual property under the traditional legal rules discussed in Part ID, *supra*.

The better view is that § 365(n)'s protections do encompass license rights to "future changes" in the

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13. The Seventh Circuit concluded FutureSource's license rights were dischargeable even where the license was assumed and sold, contrary to long established precedent that duties under executory contracts are not "debts" where the contracts remain in force and no "claim" arises unless and until the debtor rejects such a contract, surrendering all rights thereunder. *In Re National Gypsum*, 208 F.3d 498, 509; *Consolidated Gas Elec. Light & Power Co. v. United Rys. & Elec. Co.*, 85 F.2d 799, 804 (4th Cir 1936) (claim under "executory contract does not arise . . . until the contract has been rejected"). *Accord Wainer v. A.J. Equities, Ltd.*, 984 F.2d 679, 685 (5th Cir. 1993); *Federal's, Inc. v. Edmonton Inv. Co.*, 555 F.2d 577, 581 (6th Cir. 1977). *See also Vern Countryman, Executory Contracts In Bankruptcy*, 58 Minn. L. Rev. 479, 561-62 (1973) (courts generally conclude that "nonaction." *i.e.*, failure to assume or reject executory contract "means nondischargeability").

intellectual property of the type presented here. Robert Canavan, *Unsolved Mysteries of Section 365(n) — When a Bankrupt Technology Licensor Rejects an Agreement Granting Rights to Future Improvements*, 21 Seton Hall L. Rev. 800 (1991). True, there are statements in the legislative history that the protections of licensees' rights provided by § 365(n) will extend only to "existing intellectual property" and "the underlying intellectual property as it existed at the time [the bankruptcy petition is filed]." *E.g.*, S. Rep. No. 100-505, at 8-9; 43a-44a. The *statutory* language, however, refers to the licensee's "*rights*" to intellectual property under the executory contract "as such *rights* existed immediately before the case commenced. . . ." 11 U.S.C. § 365(n)(1)(B) (emphasis added).

The type of "future" intellectual property here does not involve a licensor's obligation to make changes in the licensed property (such as correction of defects, product improvements and upgrades, or provision of updated information). Rather, FutureSource's licensed right to updated information is the right to use and distribute the information (as processed through existing computer software) *if* the licensor independently chooses to produce it for other purposes (such as to sell to its own retail customers). *See* p. 2, *supra*.[14] This right is like that of the licensee of Microsoft Windows XP™ — that is, a right to receive software upgrades if the software licensor chooses to develop them.

There is no indication in the legislative history that Congress focused upon this type of "future" intellectual

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14. As the Seventh Circuit's opinion puts it, FutureSource's right with respect to updated information is to "the data specified in the contract as and when those data were created." 8a

property. What is clear is that Congress' intended distinction in providing the § 365(n) protections was between *active* and *passive* future obligations of the licensor. If the debtor/ trustee rejects an executory contract licensing intellectual property, the licensee is not able under § 365(n) to require the licensor to perform affirmative contractual obligations, such as "continued research to improve licensed intellectual property" or "defend[ing] the licensee against a [patent] infringement claim." S. Rep. No. 100-505, at 8, 9; 44a-45a. On the other hand, "performance of covenants requiring no action by the trustee imposes no burden on the estate and results in equity to the non-breaching [licensee] and certainty to the economy as a whole." *Id.* at 8; 44a. Performance of obligations like those presented here — which are only to allow the licensee *access* to improvements or other changes if the licensor independently chooses to create them — falls on the "passive" side of this balance and therefore is within the scope of § 365(n)'s protections. *Accord* Canavan, *supra*, 21 Seton Hall L. Rev. at 815, 817-18, 830-31.

This view of the scope of § 365(n)'s protections is further supported by Congress' specifically wording the statute so as to protect licensee rights that are contingent upon future events, "such as the FDA approval or issuance of the patent." S. Rep. No. 100-505, at 8; 44a. It is also supported by the admonition that "courts interpreting [§ 365(n)] should be sensitive to reasonable practices that have and will evolve among [contracting] parties seeking to add to the technological and creative wealth of America." *Id.* at 9; 46a.

Furthermore, the Seventh Circuit's decision is wrong even if § 365(n)'s protections were construed not to encompass a licensee's rights to access to improvements and

other intellectual property changes that the licensor independently decides to make. As the opinion below says, FutureSource's license rights include the computer software used to process the continuously updated raw information. 2a. That software is "existing" intellectual property and hence protected under any view of § 365(n)'s scope.[15] FutureSource's license rights are also *exclusive* as to two of the Bridge Products and specific categories of customers. *See* p. 2, *supra*. Therefore, even if § 365(n) did not protect FutureSource's right to updated information that Bridge/Reuters independently generates, FutureSource would still have the right to *stop Reuters from using the software* to provide Bridge Products to areas and customers that the licenses reserve exclusively to FutureSource. The statute is crystal clear that § 365(n)'s protections include the licensee's continuing rights to enforce exclusivity provisions. 11 U.S.C. § 365(n)(1)(B); *see also* S. Rep. No. 100-505, at 9; 45a.

> Thus, even without the benefit of a licensor improvement clause, a licensee who has retained its rights under section 365(n)(1)(B) to enforce an exclusivity provision may have the right, under patent or copyright law, to preclude the debtor from using or licensing the debtor's own post-petition improvements or derivative works. While this right does not itself allow the licensee to use the improvement, it would be an effective tool

15. Thus, although hardly controlling on the § 365(n) intellectual property issue, Judge Posner's real estate analogy concerning "property that does and does not exist" fails on its own terms. Like land with "uncompleted" buildings (in which a present leasehold may exist, 8a), the license covers presently existing software used to process continuously updated data.

> for the non-debtor to use in negotiating licenses for the use of the improvement.

Canavan, *supra*, 21 Seton Hall L. Rev. at 823 (footnote omitted); *see id.* at 821-23.

Perversely, the Seventh Circuit's alternative holding excludes *all* of a licensee's intellectual property rights from § 365(n) protection merely because a *portion* of the rights concern so-called "future" property. There is no basis in reason, much less the statutory language, for that result.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX

APPENDIX A — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT DATED NOVEMBER 27, 2002

IN THE
UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

No. 02-2060

FUTURESOURCE LLC,

Plaintiff-Appellee,

v.

REUTERS LIMITED; REUTERS S.A.; and
REUTERS AMERICA INC.,

Defendants-Appellants.

Appeal from the United States District Court for the
Northern District of Illinois, Eastern Division.
No. 02 C 2073—Elaine E. Bucklo, *Judge.*

ARGUED OCTOBER 18, 2002—
DECIDED NOVEMBER 27, 2002

Before POSNER, DIANE P. WOOD, and EVANS, *Circuit Judges.*

POSNER, *Circuit Judge.* The defendants in this diversity suit for breach of contract and tortious interference with contract (affiliated corporations that we'll call "Reuters") appeal from

the grant of a preliminary injunction to the plaintiff, FutureSource. The appeal raises issues of copyright and bankruptcy law, as well as of the common law of Illinois—actually there's no discussion of choice of law issues, and so we apply the law of the forum state. We note preliminarily that the district court based its decision entirely on an unreported district court decision from another circuit, that FutureSource places great reliance on that decision, and that Reuters is at pains to distinguish it. The reasoning of district judges is of course entitled to respect, but the decision of a district judge cannot be a controlling precedent. E.g., *Colby v. J.C. Penney Co.*, 811 F.2d 1119, 1124 (7th Cir. 1987); *Anderson v. Romero*, 72 F.3d 518, 525 (7th Cir. 1995). The law's coherence could not be maintained if district courts were deemed to make law for their circuit, let alone for the nation, since district courts do not have circuit-wide or nationwide jurisdiction.

The facts of this case are not in dispute; simplified, they are as follows. The Reuters news service provides news and financial information to paying subscribers, such as newspapers. Bridge Information Services was, and FutureSource is, a competitor of Reuters. In 1999, FutureSource made a contract with Bridge, the "Intercompany Service Agreement" (ISA), under which, in exchange for royalties of roughly $1.5 million a year, Bridge agreed to furnish FutureSource with continuously updated, consolidated, rearranged, and reformatted financial-markets data for resale to FutureSource's customers, and also with the software necessary to download the data. The agreement was to remain in force essentially as long as FutureSource wanted it to.

Appendix A

Two years after the making of the Intercompany Service Agreement, Bridge filed for bankruptcy. The bankruptcy court conducted an auction of Bridge's assets at which Reuters bought the assets used in Bridge's financial-markets data service for $275 million, pursuant to an asset purchase agreement between the parties. The agreement provided that Reuters was assuming no contractual or other obligations of Bridge other than those specified. Bridge's obligations under the Interservice Company Agreement were not among those specified; and in its order approving the sale the bankruptcy court stated that Reuters was taking the Bridge assets free and clear of all "liens, claims, interests and encumbrances." FutureSource was not a party to the bankruptcy proceeding, but it was what is called "a party in interest," which is "anyone holding a direct financial stake in the outcome of the [bankruptcy] case," *7 Collier on Bankruptcy* ¶ 1109.01[1], p. 1109-4 (15th ed. 2002), and as such it had a right to "raise and . . . appear and be heard on any issue" in the case. 11 U.S.C. § 1109(b). The right would not have been worth much to FutureSource had it not known about the auction or the asset purchase agreement, but it was notified of both and had access to a copy of the agreement yet it did not object to the sale or challenge the bankruptcy court's order. The asset purchase agreement specified that one of the assets to be sold to Reuters was the intellectual property of Bridge used in the provision of the data service that Reuters was buying.

Among the assets of Bridge that were *not* bought by Reuters (or by anyone else) at the auction were the rights conferred on Bridge by the Intercompany Service Agreement, including the right to receive royalties from FutureSource in exchange for providing the service that the agreement

required Bridge to provide to that company. At a subsequent stage in the bankruptcy proceeding those assets were sold to another company, Moneyline Network, as part of an assignment of the agreement to that company. So Moneyline became the obligee of FutureSource's royalty obligation under the ISA to Bridge and the obligor of Bridge's service obligation to FutureSource. Moneyline assured the bankruptcy court that it would perform its obligations to FutureSource under the agreement, but apparently it has not done so and, as far as we know, FutureSource is not paying Moneyline the royalties called for by the agreement—understandably, if it's receiving no services from Moneyline.

FutureSource brought this suit to compel Reuters to continue providing the service that Bridge provided to FutureSource under the Intercompany Service Agreement. FutureSource also argues that Reuters interfered tortiously with FutureSource's contracts with FutureSource's own customers by telling them that Reuters was terminating the Bridge service (which, remember, FutureSource had been reselling to them). But this claim fails if Reuters was telling them truthfully that it was merely exercising a legal right. *Soderlund Bros., Inc. v. Carrier Corp.*, 663 N.E.2d 1, 10- 11 (Ill. App. 1995); *Delloma v. Consolidation Coal Co.*, 996 F.2d 168, 172-73 (7th Cir. 1993) (Illinois law); *George A. Fuller Co. v. Chicago College of Osteopathic Medicine*, 719 F.2d 1326, 1332 (7th Cir. 1983) (same); *Worldwide Primates, Inc. v. McGreal*, 26 F.3d 1089, 1092 (11th Cir. 1994); *Allen v. Safeway Stores Inc.*, 699 P.2d 277, 279-80 (Wyo. 1985); *Restatement (Second) of Torts* § 772(a) (1979). So all that has to be decided is whether Reuters is obligated to furnish the Bridge data service to FutureSource free of charge until the end of time.

Appendix A

Nonsensical interpretations of contracts, as of statutes, are disfavored. *Level 3 Communications, Inc. v. Federal Ins. Co.*, 168 F.3d 956, 958 (7th Cir. 1999); *Health Cost Controls of Illinois, Inc. v. Washington*, 187 F.3d 703, 711-12 (7th Cir. 1999); *Outlet Embroidery Co. v. Derwent Mills*, 172 N.E. 462, 463 (1930) (Cardozo, C.J.); see also *Public Citizen v. U.S. Dept. of Justice*, 491 U.S. 440, 453-54 (1989); *Green v. Bock Laundry Machine Co.*, 490 U.S. 504, 527 (1989) (Scalia, J., concurring). Not because of a judicial aversion to nonsense as such, but because people are unlikely to make contracts, or legislators statutes, that they believe will have absurd consequences. This principle is apt to the present case. Even though the Intercompany Service Agreement, the source of FutureSource's claim, required FutureSource to pay annual royalties of $1.5 million to continue receiving the Bridge data service, FutureSource intends to pay nothing at all for the service—not to Reuters, with which it has no contract, and probably not to Moneyline, from which it apparently is receiving no service. FutureSource does not and cannot contend that it provided anything of value to Reuters in exchange for the gift of a lifetime of free data service; it has provided nothing at all (except for an interim period during which the parties were negotiating, ultimately unsuccessfully, to settle their dispute). It would be a serious indictment of American law if somehow contract, copyright, and bankruptcy law combined, like an explosive mixture of innocuous chemicals, to produce the result for which FutureSource contends.

We are not altogether certain that FutureSource is not paying and will not pay Moneyline, but its position would be hardly more sensible if it acknowledged an obligation to

pay Moneyline for services received from Reuters. Moneyline would be receiving payment for nothing, and Reuters would be rendering valuable services for nothing.

The argument that FutureSource makes on behalf of these results is that the Intercompany Service Agreement gave it a license to use Bridge's intellectual property and that an intellectual-property license, like a tenancy in real estate, is not extinguished by the sale of the underlying property. This is true in general; and we may further assume that the contract did convey to FutureSource an interest in intellectual property. Although data are not copyrightable, compilations of data that involve a significant element of creativity are, *Feist Publications, Inc. v. Rural Telephone Service Co.*, 499 U.S. 340, 348, 358-59 (1991); 17 U.S.C. §§ 101, 103, and for all we know that is the character of the Bridge data service, on which Bridge owns a copyright the validity of which is not challenged. No matter. The bankruptcy court's sale order, consistent with 11 U.S.C. § 363(f), extinguished all "interests" in the assets acquired by Reuters, and this included an interest in the intellectual property that Reuters acquired from Bridge. Although the statute does not define "interest," leaseholds are an interest, e.g., *In re Downtown Athletic Club*, No. M-47 (JSM), 2000 WL 744126, at *4 (S.D.N.Y. 2000); *In re Taylor*, 198 B.R. 142, 161-62 (Bankr. D.S.C. 1996), and leaseholds are FutureSource's own chosen analogy to Bridge's license. It is true that the Bankruptcy Code limits the conditions under which an interest can be extinguished by a bankruptcy sale, but one of those conditions is the consent of the interest holder, and lack of objection (provided of course there is notice) counts as consent. E.g., *In re Tabone, Inc.*, 175 B.R. 855, 858 (Bankr. D.N.J. 1994); *In re Elliot*,

94 B.R. 343, 345-46 (Bankr. E.D. Pa. 1988); see also *Veltman v. Whetzal*, 93 F.3d 517, 520 (8th Cir. 1996); contra, see *In re Roberts*, 249 B.R. 152, 154-57 (Bankr. W.D. Mich. 2000). It could not be otherwise; transaction costs would be prohibitive if everyone who *might* have an interest in the bankrupt's assets had to execute a formal consent before they could be sold.

And in any event the order approving a bankruptcy sale is a judicial order and can be attacked collaterally only within the tight limits that Fed. R. Civ. P. 60(b) imposes on collateral attacks on civil judgments. *In re Edwards*, 962 F.2d 641, 643-44 (7th Cir. 1992); *La Preferida, Inc. v. Cerveceria Modelo, S.A. de C.V.*, 914 F.2d 900, 908 (7th Cir. 1990); *In re Met-L-Wood Corp.*, 861 F.2d 1012, 1016, 1017-18 (7th Cir. 1988). FutureSource has made no effort to bring itself within those limits; and now that more than a year has passed since the order was issued, it is doubtful, to say the least, that FutureSource could succeed in such a collateral attack.

There is an independently fatal flaw in FutureSource's position. It fails to distinguish between property that does and property that does not exist. Suppose a builder promises to lease to someone space in a building that the builder is planning to build. That is a promise to create a leasehold; it is not a leasehold, that is, an interest in real estate (an "estate in land," as it used to be called)—there is no real estate. *Target Stores, Inc. v. Twin Plaza Co.*, 153 N.W.2d 832, 840-41 (Minn. 1967); *Wright v. Baumann*, 398 P.2d 119, 122 (Ore. 1965). It is true that *In re Wonderfair Stores, Inc. of Arizona*, 511 F.2d 1206, 1210-12 (9th Cir. 1975), and *Kmart Corp. v.*

First Hartford Realty Corp., 810 F. Supp. 1316, 1326-27 (D. Conn. 1993), seem contrary (though recall our opening remarks about the precedential significance of district court decisions). But *Wonderfair* involved uncompleted rather than nonexistent buildings, and in both cases the lease covered land, which of course did exist, as well as structures. The legal understandings that distinguish a lease from an ordinary contract have reference to existing property, improved or unimproved, owned by one party and occupied (or to be occupied) by the other.

In the Intercompany Service Agreement, Bridge merely promised to license to FutureSource data specified in the contract as and when those data were created. If as we greatly doubt the license was not extinguished by the bankruptcy sale, all this means is that FutureSource remains free to use the data that it acquired from Bridge (stale data having little, maybe no, current value). Its contractual rights under the ISA, including the right to receive licenses of future data, run against Moneyline, by virtue of Moneyline's purchase of the ISA. FutureSource has no contractual rights against Reuters, with which it has no contract; and it has no license in data that Bridge-Reuters has not yet created.

FutureSource argues that if the agreement is deemed an executory contract to grant it future licenses (executory because the duty to perform had not yet materialized), the contract survived the bankruptcy sale because it was not rejected by the trustee. 11 U.S.C. § 365(a); *In re Midway Airlines, Inc.*, 6 F.3d 492, 494 (7th Cir. 1993). (Since, for these purposes, an unexpired lease is, with respect to its unexpired portion, a contract, *In re Boston Post Road Ltd.*

Partnership, 21 F.3d 477, 484 (2d Cir. 1994), FutureSource's argument is actually independent of whether the Intercompany Service Agreement created an interest that is the legal equivalent of a leasehold.) Of course the agreement was not rejected—it was assigned to Moneyline. Any rights that FutureSource has under it are, as a result of the assignment, rights against Moneyline, not against Reuters. The agreement did not forbid assignment, and even if it had forbidden it the bankruptcy court would not have been bound. 11 U.S.C. § 365(f)(1); *In re Midway Airlines, Inc., supra*, 6 F.3d at 495-96; *In re Headquarters Dodge, Inc.*, 13 F.3d 674, 682 (3d Cir. 1993); Douglas G. Baird, *The Elements of Bankruptcy* 124-25 (3d ed. 2001).

Obviously a preliminary injunction should not be entered if the plaintiff has no claim; and FutureSource has none. The next step in the district court presumably will be the filing of a motion for summary judgment by Reuters and its grant by the district judge. But we decline to anticipate the judge's ruling on such a motion (and have not been asked to do so).

REVERSED.

A true Copy:

Teste:

_____

Clerk of the United States Court of Appeals for the Seventh Circuit

APPENDIX B — ORDER OF ENTRY OF PRELIMINARY INJUNCTION OF THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS, EASTERN DIVISION DATED APRIL 25, 2002

IN THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS — EASTERN DIVISION

No. 02 C 2073

Judge Bucklo

Magistrate Judge Levin

FUTURESOURCE LLC,

Plaintiff,

v.

REUTERS LIMITED; REUTERS S.A.; and REUTERS AMERICA INC.,

Defendants.

ORDER OF ENTRY OF PRELIMINARY INJUNCTION

This cause coming to be heard on Plaintiff FutureSource LLC's ("FutureSource") Motion for Preliminary Injunction against Defendants Reuters Limited, Reuters SA, and Reuters America Inc. (collectively "Reuters"), due notice having been

given, the parties being represented by counsel, the Court having issued its Memorandum Opinion and Order of April 12, 2002, granting the Preliminary Injunction, and the Court being fully advised in the premises:

IT IS HEREBY ORDERED THAT:

1. FutureSource has established the likelihood of a license to sell the commodities information products described in the Verified Complaint as the Bridge Products;

2. Reuters, pursuant to FutureSource's licenses for the Bridge Products, is obligated to provide the Bridge Products to FutureSource's customers;

3. Reuters intended to cease providing the Bridge Products to FutureSource's customers after April 1, 2002;

4. If Reuters cuts off service of the Bridge Products to FutureSource's customers, it would be interfering with FutureSource's license rights and customer contracts;

5. In addition, Reuters has solicited FutureSource's customers to have them contract with Reuters for provision of the Bridge Products after March 27, 2002;

6. Reuters' conduct will cause FutureSource to lose customers to Reuters and other third party competitors;

7. FutureSource is likely to succeed on the merits of its claim for tortious interference with contract and breach of contract against Reuters;

8. FutureSource is without an adequate remedy at law. Due to the loss of its customers, FutureSource will suffer irreparable harm if a Preliminary Injunction is not granted;

9. In weighing the harms to each party from the entry of the Preliminary Injunction, the Court finds that FutureSource will suffer more if the requested relief is not granted than Reuters will suffer if it is granted; and

10. The public interest weighs in favor of the entry of the Preliminary Injunction.

ACCORDINGLY, IT IS HEREBY ORDERED THAT:

1. The Temporary Restraining Order of March 29, 2002, as amended on April 5, 2002, is hereby converted into a Preliminary Injunction and shall be entered against Reuters to maintain the *status quo* between the parties;

2. Reuters shall be enjoined from terminating its provision of the Bridge Products to FutureSource's customers. Reuters must continue to provide the Bridge Products, and all necessary services therewith, in a timely and professional manner to FutureSource's customers;

3. Reuters is enjoined from speaking or corresponding with customers who obtained the BridgeFeed, BridgeStation or BridgeChannel products and services (the "Bridge Services") from FutureSource under the terms of the Intercompany Services Agreement to inform them that Reuters can discontinue their receipt of the Bridge Services,

and regarding replacing those Bridge Services with Bridge Services or products with substantially similar content provided by Reuters.

4. This Preliminary Injunction shall remain in effect until final judgment on the merits or future Court order, subject to any appeal of this Order pursuant to 28 U.S.C. § 1292(a)(1);

5. FutureSource shall be required to post security in the amount of $300,000 in conjunction with the entry of this Preliminary Injunction.

6. This matter is set for status on May 10, 2002 at 10:00 A.M.

ENTERED

s/ Elaine E. Bucklo
The Honorable Judge Elaine E. Bucklo

DATED: 4-25-02

APPENDIX C — PRELIMINARY INJUNCTION ORDER OF THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS, EASTERN DIVISION DATED APRIL 12, 2002

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

No. 02 C 2073

FUTURESOURCE LLC,

Plaintiff,

REUTERS LIMITED; REUTERS SA; and
REUTERS AMERICA, INC.,

Defendants.

PRELIMINARY INJUNCTION ORDER

Futuresource ("FS") (re)sells data and software to the commodities industry. It obtained its products from Bridge Information Systems ("Bridge") under licenses pursuant to a 1999 Intercompany Agreement ("ISA"). Bridge declared bankruptcy in February 2001, and Reuters bought the Bridge products at a bankruptcy auction, purportedly excluding, with the approval of the bankruptcy court in Missouri, certain software at issue here (the "products"), and "all interests" held by Bridge in its ISA with FS. In August 2001, Moneyline Network ("Moneyline") was assigned Bridge's interest in the FS/Bridge license to the products. In September 2001, Reuters agreed to sell FS the software for a brief period.

Near the expiration of that period, in March 2002, Reuters notified FS that it would not renew the interim agreement or allow FS to use the products anymore. It began contacting FS's customers to inform them of this. FS asked me for a TRO, which I granted. It now asks for a preliminary injunction, which I also grant.

The main issue is likelihood of success on the merits. My reasoning in granting the TRO was fairly straightforward. The ISA was an executory contract that remains in effect unless it was rejected by the bankruptcy trustee, under 11 U.S.C. § 365(a), and it is undisputed that neither the ISA nor the licenses were rejected by the bankruptcy trustee. They were assigned to Moneyline, although Bridge owns the products (the software) to which Moneyline holds the licenses. The ISA and licenses therefore bind FS and whoever stands in Bridge's shoes, namely Moneyline, but because the licenses *are licenses to the products that Bridge owns*, Bridge took subject to the licenses because they were not rejected. The bankruptcy court's order purporting to sell Bridge the products free and clear therefore failed to do so in this respect, because the licenses to the products were not rejected. *See In re Novon International*, Nos. 98-CV-0677E(F), 96-BK-15463B, 2000 WL 432848 (W.D.N.Y. Mar. 31, 2000). "[T]he new patent holder takes title subject to the license agreements, whether it affirmatively 'assumes' them or not." *Id.* at *6.

Reuters attempts to distinguish Novon by saying that the ISA and the licenses are a services contract, rather than one concerning the rights to intellectual property-here software, there a patent. But specific performance is not the issue.

Appendix C

At issue here are precisely licenses to software, not services. All Reuters must do is honor the licenses, while Moneyline performs the ISA. Reuters also argues that if anyone inherited the obligations of the licenses, it is Moneyline. That is true, but Reuters' interest in the products is subject to Moneyline's licenses. Reuters also contends that any agreements it had with FS are extinguished by the terms of the interim agreement, now expired, referring me to the integration clause thereof. However, this clause cannot extinguish FS's licenses, because FS has none, or Moneyline's licenses, because Moneyline was not a party to the interim agreement. The integration clause merely states that the written terms of that agreement were the only terms. It is irrelevant to the licenses.

For the rest, Reuters, occupies itself mainly with arguing that the review of, the bankruptcy court's assets sale is outside my jurisdiction because FS did not object to the bankruptcy court. However, FS was not a creditor of Bridge. Although the proceeds of executory contract are "accounts" for the purposes of establishing a security interest, *see* UCC § 9-106, *J. Catton Farms, Inc. v First Nat. Bank of Chicago*, 779 F.2d 1242, 1248 (7th Cir, 1983), proceeds are not at issue here. An executory contract by itself is not per se a lien or debt. Since FS was not a creditor but only a contracting party with the debtor, it could not object in bankruptcy court. The same argument refutes Reuters' arguments that the matter is res judicata because there was no objection in that court, or that a collateral attack on the bankruptcy court's judgment is barred by FS's silence there. The bankruptcy court order barring lawsuits against Reuters to recover claims against

Bridge is not relevant: FS does not seek to recover a claim against Bridge. It has a claim that is "independently assertable against [Reuters]," in the language of the order.

Reuters objects that FS is unlikely to succeed on its tortious interference claim because Reuters interference with FS' s customers was unjustified. However, this depends on whether Reuters took the product subject to the licenses; I have held it did.

Reuters' arguments as to, the other requirements for a preliminary injunction are slight. There was no undue delay, because Reuters did not know until March 2002 that Reuters had no intention to renew the interim agreement. The injunction would indeed preserve the status quo; the fact that FS does not have a license from Reuters is a nonissue. The injunction will not give it one. Moneyline holds the licenses. FS does not have unclean hands; it has every right to seek relief here; and if Reuters can show that FS has not paid for the use of licenses under the interim agreement, Reuters may sue for breach. There is no adequate remedy at law: FS has shown that it is likely to lose goodwill and customers if Reuters cuts it off or solicits its customers. Reuters' arguments concerning public interest and the balance of hardships depend on the cogency of its arguments against the likelihood that FS will succeed on the merits, which I do not accept. The preliminary injunction is granted.

ENTER ORDER:

s/ Elaine E. Bucklo
Elaine E. Bucklo
United States District Judge

Dated: April 12, 2002

APPENDIX D — AGREED ORDER AMENDING ORDER OF MARCH 29, 2002 OF THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS, EASTERN DIVISION DATED APRIL 5, 2002

IN THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS — EASTERN DIVISION

No. 02 C 2073

Judge Bucklo

Magistrate Judge Levin

AGREED ORDER AMENDING ORDER OF MARCH 29, 2002

This cause coming to be heard on Defendants' Emergency Motion to Amend Order of March 29, 2002, due notice having been given, and the Court being fully advised in the premises:

IT IS HEREBY ORDERED THAT:

This Court's Order for Entry of Temporary Restraining Order, dated March 29, 2002, is amended as follows, *nunc pro tunc* March 29, 2002:

> Paragraph 3 on page 2 is revised to read, "3. Reuters is enjoined from speaking or corresponding with customers who obtained the BridgeFeed, BridgeStation or BridgeChannel

products and services (the "Bridge Services") from FutureSource under the terms of the Intercompany Services Agreement to inform them that Reuters can discontinue their receipt of the Bridge Services, and regarding replacing those Bridge Services with Bridge Services or products with substantially similar content provided by Reuters."

Dated: 4/5, 2002

ENTERED

s/ Elaine E. Bucklo
The Honorable Judge Elaine E. Bucklo

APPENDIX E — MEMORANDUM OPINION AND ORDER OF THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS, EASTERN DIVISION DATED MARCH 29, 2002

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

No. 02 C 2073

FUTURESOURCE LLC,

Plaintiff,

v.

REUTERS LIMITED; REUTERS SA;
and REUTERS AMERICA, INC.,

Defendants.

MEMORANDUM OPINION AND ORDER

In March, 1999, FutureSource/Bridge LLC, an Illinois corporation, entered a contract with Bridge Information Systems, Inc., a Missouri corporation, under which Bridge granted FS/B an exclusive license to sell a desktop software called BridgeStation Products to commodity traders and others. The contract (referred to herein as the Intercompany Agreement) was still in effect when Bridge declared bankruptcy under chapter 11 of the United States Bankruptcy Code in 2001. The Trustee in bankruptcy sold most of Bridge's assets to Reuters Ltd. and related companies,

specifically including BridgeStation software. Schedule 1A. The Reuters contract excluded "All interests held, directly or indirectly, by [Bridge] . . . . in Future Source/Bridge LLC and the entire assets, including all contracts relating thereto, and business operations thereof." Schedule 2.1(b), par. 3. Section 2.7(a) of the Reuters contract purported to exclude all obligations of Bridge that relate to any of the Excluded Assets. Clearly, therefore, Reuters attempted to avoid any responsibility for its obligation to provide software under the Intercompany Agreement. The Reuters contract was approved by the bankruptcy court in September, 2001 (as I understand it, preliminary approval was given in May, but changes were thereafter made and final approval did not come until September 21, 2001).

In August, 2001, the Trustee purported to sell to MoneyLine Network, Inc. Bridge's interest in the Future/Source/Bridge license. Thereafter, Future/Source and Reuters entered into an agreement in September, 2001, for a short duration, under which Future/Source purchased rights to use the BridgeStation software from Reuters. When Reuters announced that it would not continue the agreement, and began contacting Future/Source customers, Future/Source sued. This court has jurisdiction pursuant to 28 U.S.C. § 1332. Future/Source argues that Reuters is interfering with its contractual relationships with its customers and also that Reuters must continue providing the BridgeStation software under Section 365 of the Bankruptcy Code because notwithstanding Reuters' attempts to avoid any obligations under the 1999 contract, according to Future/Source Reuters did not follow proper procedure for rejecting the

contract, which would have given Future/Source certain rights. The answer is a matter of bankruptcy law.

Future/Source argues that it had to receive notice that the contract was going to be rejected, which of course it did not because the contract was instead assumed and transferred. It did receive notice of certain bid procedures, but it is unclear that the notice was specific enough to charge it with knowledge of the contract provisions. Furthermore, prior to final approval of the contract, the bankruptcy court had approved the transfer of the Intercompany Agreement to MoneyLine. Reuters was given notice of the Trustee's assumption of the Intercompany Agreement and its assignment to MoneyLine. Under 11 U.S.C. § 365, since the agreement was not rejected, it remains in effect. Accordingly, Reuters remains obligated under the contract. See e.g., *In re Novon International, Inc.* 2000 WL 4332848 (W.D.N.Y. 2000).

Since, as I understand the law applicable to the conflicting claims and interests of the parties, Future/Source seems likely to prevail, it has met the first requirement for issuance of a temporary restraining order against Reuter's interference with its contracts with its customers. The remaining criteria for issuance of a temporary restraining order are well known and are met in this case. *See, e.g., Ty, Inc. v. Jones Group, Inc.*, 237 F.3d 891, 895 (7th Cir. 2001). Plaintiff has no adequate remedy at law and will suffer irreparable harm if the order is not granted. The balance of hardships also favors plaintiff since without the order, it will immediately lose its contractual relationships. Nor if the public interest likely to be adversely

affected by grant of the order. (Reuters has not argued that any of these requirements are not met, arguing only that Future/Source has not shown a likelihood of success on the merits.) Accordingly, the temporary restraining order will issue. If Reuters believes there are factual issues that could affect the grant of a preliminary injunction (as it seemed to indicate at the hearing today), it shall identify them within one week. Otherwise, this order will be extended to a preliminary injunction at the end of ten days since the parties have had sufficient time to brief the legal issue.

ENTER ORDER:

s/ Elaine E. Bucklo
Elaine E. Bucklo
United States District Judge

Dated: March 29, 2002

Appendix E

IN THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF ILLINOIS EASTERN DIVISION

Cause No. 02 C 2073

FUTURESOURCE LLC,

Plaintiff,

v.

REUTERS LIMITED; REUTERS SA; and REUTERS AMERICA, INC.,

Defendants.

ORDER FOR ENTRY OF TEMPORARY RESTRAINING ORDER

This cause coming to be heard on Plaintiff FutureSource LLC's ("FutureSource") Motion for Temporary Restraining Order and Preliminary Injunction against Defendants Reuters Limited, Reuters SA, and Reuters America, Inc. (collectively "Reuters"), due notice having been given, the parties being represented by counsel, and the Court being fully advised in the premises:

IT IS HEREBY ORDERED THAT:

1. FutureSource has established the likelihood of a license to sell the commodities information products described in the Verified Complaint as the Bridge Products;

2. Reuters, pursuant to FutureSource's licenses for the Bridge Products, is obligated to provide the Bridge Products to FutureSource's customers;

3. Reuters intends to cease providing the Bridge Products to FutureSource's customers after April 1, 2002;

4. If Reuters cuts off service of the Bridge Products to FutureSource's customers, it would be interfering with FutureSource's license rights and customer contracts;

5. In addition, Reuters has solicited FutureSource's customers to have them contract with Reuters for provision of the Bridge Products after March 27, 2002;

6. Reuters' conduct will cause FutureSource to lose customers to Reuters and other third party competitors;

7. FutureSource is likely to succeed on the merits of its claim for tortious interference with contract and breach of contract against Reuters;

8. FutureSource is without an adequate remedy at law. Due to the loss of its customers, FutureSource will suffer irreparable harm if a Temporary Restraining Order is not granted;

9. In weighing the harms to each party from the entry of the Temporary Restraining Order, the Court finds that FutureSource will suffer more if the requested relief is not granted than Reuters will suffer if it is granted; and

10. The public interest weighs in favor of the entry of the Temporary Restraining Order and Preliminary Injunction.

ACCORDINGLY, IT IS HEREBY ORDERED THAT:

1. A Temporary Restraining Order shall be entered against Reuters to maintain the *status quo* between the parties;

2. Reuters shall be enjoined from terminating its provision of the Bridge Products to FutureSource's customers. Reuters must continue to provide the Bridge Products, and all necessary services therewith, in a timely and professional manner to FutureSource's customers;

3. Reuters is enjoined from soliciting or contacting FutureSource's customers in any fashion;

4. This Temporary Restraining Order shall remain in effect for ten (10) days to and including April 12, 2002, in accordance with Rule 6. FutureSource may petition this Court by April 12, 2002 to extend this Temporary Restraining Order for another such ten (10) day period of time with good cause shown;

5. FutureSource shall be required to post security in the amount of $300,000 in conjunction with the entry of this Temporary Restraining Order;

6. This matter is set for status on April 12, 2002 at 10:00 a.m.

Appendix E

ENTERED:

s/ Elaine E. Bucklo
The Honorable Judge Elaine E. Bucklo

DATED: 3/29/02

APPENDIX F — RELEVANT STATUTES

TITLE 11
CHAPTER 3
SUBCHAPTER IV

11 U.S.C. § 363

Sec. 363. – Use, sale, or lease of property

(a) In this section, "cash collateral" means cash, negotiable instruments, documents of title, securities, deposit accounts, or other cash equivalents whenever acquired in which the estate and an entity other than the estate have an interest and includes the proceeds, products, offspring, rents, or profits of property and the fees, charges, accounts or other payments for the use or occupancy of rooms and other public facilities in hotels, motels, or other lodging properties subject to a security interest as provided in section 552(b) of this title, whether existing before or after the commencement of a case under this title.

(b)(1) The trustee, after notice and a hearing, may use, sell, or lease, other than in the ordinary course of business, property of the estate.

* * *

(f) The trustee may sell property under subsection (b) or (c) of this section free and clear of any interest in such property of an entity other than the estate, only if—

(1) applicable nonbankruptcy law permits sale of such property free and clear of such interest;

(2) such entity consents;

(3) such interest is a lien and the price at which such property is to be sold is greater than the aggregate value of all liens on such property;

(4) such interest is in bona fide dispute; or

(5) such entity could be compelled, in a legal or equitable proceeding, to accept a money satisfaction of such interest.

* * *

Appendix F

TITLE 11
CHAPTER 3
SUBCHAPTER IV

11 U.S.C. § 365

Sec. 365. – Executory contracts and unexpired leases

(a) Except as provided in sections 765 and 766 of this title and in subsections (b), (c), and (d) of this section, the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor.

* * *

(h)(1)(A) If the trustee rejects an unexpired lease of real property under which the debtor is the lessor and—

(i) if the rejection by the trustee amounts to such a breach as would entitle the lessee to treat such lease as terminated by virtue of its terms, applicable nonbankruptcy law, or any agreement made by the lessee, then the lessee under such lease may treat such lease as terminated by the rejection; or

(ii) if the term of such lease has commenced, the lessee may retain its rights under such lease (including rights such as those relating to the amount and timing of payment of rent and other amounts payable by the lessee and any right of use, possession, quiet enjoyment, subletting, assignment, or hypothecation) that are in or appurtenant to the real property for the balance of the term of such lease and for any renewal or extension of such rights to the extent that such rights are enforceable under applicable nonbankruptcy law.

Appendix F

* * *

(n)(1) If the trustee rejects an executory contract under which the debtor is a licensor of a right to intellectual property, the licensee under such contract may elect—

(A) to treat such contract as terminated by such rejection if such rejection by the trustee amounts to such a breach as would entitle the licensee to treat such contract as terminated by virtue of its own terms, applicable nonbankruptcy law, or an agreement made by the licensee with another entity; or

(B) to retain its rights (including a right to enforce any exclusivity provision of such contract, but excluding any other right under applicable nonbankruptcy law to specific performance of such contract) under such contract and under any agreement supplementary to such contract, to such intellectual property (including any embodiment of such intellectual property to the extent protected by applicable nonbankruptcy law), as such rights existed immediately before the case commenced, for—

(i) the duration of such contract; and

(ii) any period for which such contract may be extended by the licensee as of right under applicable nonbankruptcy law.

(2) If the licensee elects to retain its rights, as described in paragraph (1)(B) of this subsection, under such contract—

(A) the trustee shall allow the licensee to exercise such rights;

(B) the licensee shall make all royalty payments due under such contract for the duration of such contract and for any period described in paragraph (1)(B) of this subsection for which the licensee extends such contract; and

(C) the licensee shall be deemed to waive—

(i) any right of setoff it may have with respect to such contract under this title or applicable nonbankruptcy law; and

(ii) any claim allowable under section 503(b) of this title arising from the performance of such contract.

(3) If the licensee elects to retain its rights, as described in paragraph (1)(B) of this subsection, then on the written request of the licensee the trustee shall—

(A) to the extent provided in such contract, or any agreement supplementary to such contract, provide to the licensee any intellectual property (including such embodiment) held by the trustee; and

(B) not interfere with the rights of the licensee as provided in such contract, or any agreement supplementary to such contract, to such intellectual property (including such

embodiment) including any right to obtain such intellectual property (or such embodiment) from another entity.

(4) Unless and until the trustee rejects such contract, on the written request of the licensee the trustee shall—

(A) to the extent provided in such contract or any agreement supplementary to such contract—

(i) perform such contract; or

(ii) provide to the licensee such intellectual property (including any embodiment of such intellectual property to the extent protected by applicable nonbankruptcy law) held by the trustee; and

(B) not interfere with the rights of the licensee as provided in such contract, or any agreement supplementary to such contract, to such intellectual property (including such embodiment), including any right to obtain such intellectual property (or such embodiment) from another entity.

* * *

APPENDIX G — SENATE REPORT NO. 100-505

SENATE REPORT NO. 100-505
September 14, 1988

The Committee on the Judiciary, to which was referred the bill (S. 1626) to amend title 11, United States Code, the Bankruptcy Code, regarding protection of certain intellectual property rights in bankruptcy, having considered the same, reports favorably thereon with an amendment in the nature of a substitute, and recommends that the bill, as amended, do pass.

I. PURPOSE

The purpose of the bill is to amend Section 365 of the Bankruptcy Code to make clear that the rights of an intellectual property licensee to use the licensed property cannot be unilaterally cut off as a result of the rejection of the license pursuant to Section 365 in the event of the licensor's bankruptcy. Certain recent court decisions interpreting Section 365 have imposed a burden on American technological development that was never intended by Congress in enacting Section 365. The adoption of this bill will immediately remove that burden and its attendant threat to the development of American Technology and will further clarify that Congress never intended for Section 365 to be so applied.

II. LEGISLATIVE HISTORY

On August 7, 1987, Senators DeConcini and Heflin introduced S. 1626, the Intellectual Property Bankruptcy Act. The bill's introduction focused attention on recent court

decisions addressing Section 365 of the bankruptcy code which have stripped intellectual property licensees of their right to continue to use the licensed property. Numerous meetings were held within the intellectual property and bankruptcy communities to discuss the problems and the possible solutions.

On June 10, 1988, Senator Heflin convened a hearing of the Subcommittee on Courts and Administrative Practice, and received testimony from the following witnesses: John L. Pickitt, president of Computer and Business Equipment Manufacturers Association; Steven C. Mendell, chairman and CEO of XOMA Corp.; John P. McLaughln, vice president of Genetech Inc.; George Hahn, chairman of the Executory Contracts Committee, National Bankruptcy Conference; and Jeffrey Tarkenton of the American Bankruptcy Institute.

A substitute amendment was drafted to incorporate the recommendations that evolved from the meetings and the hearings. On August 9, 1988, the Subcommittee on Courts and Administrative Practice unanimously approved the substitute amendment and on August 10, 1988, the Committee on the Judiciary unanimously reported the bill.

III. DISCUSSION

A. BACKGROUND: RECENT COURT DECISIONS

Several recent court decisions, including Lubrizol Enterprises, Inc. v. Richmond Metal Finishers, Inc., 765 F.2d 1043 (4th Cir. 1985), cert. denied 106 S.Ct. 1285 (1986), have interpreted Section 365 of the Bankruptcy Code (the

'Code') as providing a basis for permitting a licensor of intellectual property to strip its licensee of any continuing right to use the licensed intellectual property under the auspices of rejecting the license as an executory contract. Under the Code, a trustee or debtor in possession may be permitted to reject—that is, to breach—an executory contract when, in its business judgment as reviewed by the court, it concludes that affirmative ongoing performance of the contract would not be beneficial to the estate. These cases, however, have relieved the debtor not simply of its ongoing affirmative performance obligations under the executory license agreement, but also of its passive obligation to permit the licensee to use the intellectual property as provided in the license. Under this view, since rejection results in valuable rights apparently reverting to the bankruptcy estate—rights which the bankruptcy estate otherwise would have to share with the licensee—rejection will nearly always be arguably beneficial to the bankruptcy estate and any exercise of business judgment, however reviewed by the court, will lead to rejection.

This view, which several courts have not modified under their powers in equity, leaves licensees in a precarious position and thus threaten the very flexible and beneficial system of intellectual property licensing which has developed in the United States. Congress never anticipated that the presence of executory obligations in an intellectual property license would subject the licensee to the risk that, upon bankruptcy of the licensor, the licensee would lose not only any future affirmative performance required of the licensor under the license, but also any right of the licensee to continue to use the intellectual property as originally agreed in the license agreement.

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The court decisions on Section 365 that have stripped intellectual property licensees of their right to continue to use the licensed property have gained wide notice. They threaten an end to the system of licensing of intellectual property (discussed below) that has evolved over many years to the mutual benefit of both the licensor and the licensee and to the country's indirect benefits. Because of the instability that Section 365 has introduced into the licensing relations, parties who would have formerly accepted licenses—the right to use another's intellectual property—are now forced to demand assignments—outright transfer of ownership of the intellectual property. This change in basic format is wasteful and cumbersome and is especially chilling to small business technologists. It is not an overstatement to say that the change is a fundamental threat to the creative process that has nurtured innovation in the United States.

B. BACKGROUND: THE ROLE OF LICENSING

Licensing of technology, which the bill is intended to protect and to facilitate, plays a substantial role in the process of technological development and innovation. That process begins with an inventive concept and must proceed through an expensive and risky series of steps including research, development, manufacturing and marketing. At each step, both money and additional refinement of the idea are required. Often, the financing and additional refinement are only available through the participation of persons other than the original innovator.

Licensing provides the mechanism by which the original innovator can retain sufficient ownership of his innovation

so that he shares in the ultimate economic reward, while sharing that reward as remuneration tc those who would provide the financing and refinement necessary to achieve economic success. Licensing also provides a mechanism whereby the innovator who has identified more than one domain in which his invention may have application can seek partners for each field of use without risking the probability that one developer's narrow focus will deny him the rewards of development in another area.

The alternative to licensing is outright sale. If the innovator sells his innovation at its genesis, he passes the entire risk of development onto the purchaser. If the legal environment forces reliance on sale rather than licensing, the number of parties who can participate in new technological development is sharply curtailed.

When intellectual property is assigned rather than licensed, the original creator loses his personal stake. The licensee or assignee frequently is interested in the intellectual property for a specific application or geographic market. In order to assure the continued availability of the intellectual property against the contingency of the creator's bankruptcy, however, the party seeking the intellectual property for limited use must demand assignment of the property, notwithstanding that a license would otherwise serve his purpose. The creator then is either totally alienated from his creation or, at best, given a license by the assignee. Such circumstances create obvious disincentives to the full development of intellectual property. If the creator is unwilling to assign, in some instances, transactions simply are not completed. In others, the licensee discounts what he

will pay to account for the risk now seen as inherent in Section 365. In short, Section 365 is resulting in undercompensation of U.S. inventors. Ironically, the present law, as it is now being interpreted by courts, can result in increased financial distress for the inventor, causing him to be shortchanged to adjust for a risk which under present law cannot be contractually removed if a license format is selected.

C. OVERVIEW OF BILL

The bill provides for treatment of intellectual property licenses under Section 365 in a manner that parallels generally the treatment of real estate leases in the existing provisions of Section 365(h)(1). While intellectual property plays a unique role in technological and economic development, the problems associated with rejection of executory contracts are common with other special forms of property, such as real property leases. In both real estate leases and intellectual property licenses, the underlying property is unique. When the lessee or the licensee is threatened with loss of use of the property, it is not possible to obtain precise cover from another source.

In adopting the Code, Congress recognized this problem with respect to real property leases and enacted Section 365(h). That section clarified that, although a bankrupt lessor could avoid performance of future obligations under an unexpired lease, it could not cause through rejection of the lease an innocent lessee to forfeit the remainder of its leasehold. Neither the bar nor Congress then foresaw the need to protect similarly the reasonable expectations of intellectual property licensees. The bill corrects the perception of some

courts that Section 365 was ever intended to be a mechanism for stripping innocent licensee of rights central to the operations of their ongoing business and stripping the American licensing system of its dependability and flexibility. Thus, the bill does not accord special treatment for intellectual property or the interests of its licensors or licensees beyond that which Congress has recognized in the past is required for these other unique property rights. The bill recognizes that there may be circumstances in which the future affirmative performance obligations under a license cannot be performed in a manner that benefits the estate, but limits the consequences of the breach or rejection of the contract.

D. OTHER MATTERS

As discussed above, the bill is intended to respond to a particular problem arising out of recent court decisions under Section 365. As such, it is not in any way intended to address broader matters under Section 365 or the Bankruptcy Code in general. The bill does not affect the test of when a contract is an executory contract or the exercise of business judgment in rejecting an executory contract. Nor does the bill address or intend any inference to be drawn concerning the treatment of executory contracts which are unrelated to intellectual property. In addition, the bill does not treat certain issues related to intellectual property that are already dealt with elsewhere in the Code: Maintaining the confidentiality of trade secrets is adequately provided for in Section 107(b)(2); determinations of whether intellectual property licenses are assumable or assignable can be made in accordance with sections 365(c) and (f). The bill does not deal with debtor licensees.

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Finally, the bill does not address the rejection of executory trademark, trade name or service mark licenses by debtor-licensors. While such rejection is of concern because of the interpretation of section 365 by the Lubrizol court and others, see, e.g., In re Chipwich, Inc., 54 Bankr. Rep. 427 (Bankr. S.D.N.Y. 1985), such contracts raise issues beyond the scope of this legislation. In particular, trademark, trade name and service mark licensing relationships depend to a large extent on control of the quality of the products or services sold by the licensee. Since these matters could not be addressed without more extensive study, it was determined to postpone congressional action in this area and to allow the development of equitable treatment of this situation by bankruptcy courts.

IV. VOTE OF COMMITTEE

On August 10, 1988, with a quorum present, by unanimous consent, the Committee on the Judiciary, ordered the bill, as amended, reported.

* * * * *

VI. SECTION-BY-SECTION ANALYSIS

Section 1(a) amends Section 101 of the Bankruptcy Code, which sets forth definitions used in the Bankruptcy Code.

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A. NEW SECTION 101(52) OF TITLE 11, UNITED STATES CODE

The first new defined term is 'intellectual property.' The definition is a listing of types of intellectual property. The definition sets forth in some instances both the actual type of property as to which the intellectual property proprietor obtains rights (e.g., invention, process, design, confidential research or development information, work of authorship) and the alternative legal mechanism for protecting that underlying property (e.g., trade secret, patents and copyrights). The amendment broadly defines 'intellectual property' to include virtually all types of such rights (other than trademarks and similar rights) whether protected by federal or State law, statutory or common law. The bill in no way defines or alters any substantive intellectual property law, it merely refers to those rights which are already protected by applicable nonbankruptcy law. Proposed Section 101(52) makes clear that the operation of the bill is to cover both the intangible legal right associated with intellectual property and the tangible object or objects, such as books, blueprints and electronic media, in which such intellectual property may be fixed or recorded.

The definition of 'intellectual property' is unusual for a federal statute because of its inculsion of trade secret, normally a concept reserved for development by the states. Because bankruptcy processes can alter rights created by state law, this inclusion is appropriate. Also included as a separate category is confidential research or development information. This was done because some states narrowly define trade secret, but accord protection to the developer of confidential

technical information falling outside those definitions. The definition is broad and is to be interpreted liberally to carry out the intent of Congress to remove the cloud cast by that recent interpretation of the Bankruptcy Code upon the intellectual property licensing system.

B. NEW SECTION 101(53) OF TITLE 11, UNITED STATES CODE

The second new defined term is 'mask work,' a term included within the definition of 'intellectual property.' The term is used in recently adopted legislation and is to have the same meaning in title 11 as in section 901(a)(2) of title 17.

C. NEW SUBSECTION 365(N) OF TITLE 11, UNITED STATES CODE

Section (1)(b) adds a new subsection to Section 365 of title 11, United States Code, consisting of four paragraphs.

1. New paragraph (n)(1) of subsection 365(n)

The first paragraph of the new Section provides that, in the event an executory contract under which the debtor is a licensor of rights to intellectual property is rejected in the licensor's bankruptcy, the licensee may elect one of two sets of consequences to attach to that rejection. The licensee may treat the rejection as terminating the license, leaving the licensee with its various rights as a contract creditor under the Code. This course of action would be available to the licensee without this bill.

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The second alternative which the bill explicitly makes available to the licensee is to elect to retain its rights under the license, as such rights existed immediately before the case commenced. The bill recognizes that continued affirmative performance of an intellectual property license may be impractical; for instance, a trustee will generally be unable to perform covenants calling for continued research to improve licensed intellectual property. However, performance of covenants requiring no action by the trustee impose no burden on the estate and result in equity to the nonbreaching party and certainty to the economy as a whole. When a bankruptcy court finds rejection of an intellectual property license to be appropriate, if the licensee so elects, the bill protects the licensee's right to the intellectual property as it existed at the time of the filing. If the licensee elects to retain such rights, he is required to continue making all royalty payments due under the rejected license, as more fully described below.

It is important to note that the amendment, when referring to retention of rights under 'such contract,' deliberately omits the phrase 'the term of which has commenced' appearing in the somewhat parallel subsection 365(h) in connection with leases and time share plans. Frequently, the term of the license agreement is contingent upon the occurrence of a future event, such as FDA approval or issuance of the patent. The benefits of the bill are intended to extend to such license agreements, consistent with the limitation that the licensee's rights are only in the underlying intellectual property as it existed at the time of the filing.

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For the term of the rejected license and any period for which such license could have been extended, the licensee under the rejected license.

(1) is entitled to use the underlying intellectual property in the state that it existed on the day of the bankruptcy filing as provided in the license and

(2) is entitled to any judicial relief necessary to enforce that set of rights.

For instance, if the contract granted exclusive use to the licensee, such exclusivity would be preserved to the licensee. To this extent, the licensee is given the right to compel specific performance, i.e., to enjoin the licensing to another of the rights granted by the contract to the licensee. Retention of contractual rights, both in extent and quality, is a central aim of the bill. If the trustee has chosen to reject the license, the licensee, although entitled to elect to retain the use of the existing intellectual property without interference, cannot otherwise compel affirmative post-petition performance under the license. For instance, the licensee could not compel the licensor to defend the licensor's patent against an infringement claim. If the license provided the licensee a right to defend such a claim, however, that is one of the rights which this bill would protect.

Intellectual property licensing arrangements are not generally standardized. Rather, the particular transaction is the product of the circumstances of the licensor, the licensee and other interested parties. It is not unusual for the licensing arrangements to involve parties other than the licensor and

licensee. It is also not unusual for the license agreement to be one of several agreements governing the working relationship between the licensor and licensee. For instance, the licensor may have contracted to supply the licensee with a product incorporating the licensed intellectual property and may have agreed that the licensee would only have access to information necessary to produce the licensed intellectual property in the event of the licensor's inability or unwillingness to supply the licensee. To assure the licensee of access to such secret information at the defined time, the licensor may have agreed to turn over such information to a third party to be held in escrow until the triggering event. The third-party escrow agent would be a party to such an agreement, and the agreement would be set forth in a document separate from the basic license. Section 365(n)(1)(B), thus, speaks of the retention by the licensee of rights to the intellectual property under 'any agreement supplementary to such contract.' The licensee retains both the rights set forth in the rejected license itself and any agreement supplementary thereto, whether the supplementary agreement was itself the subject of a rejection by the trustee. This bill is intended to restore confidence in the system of intellectual property licensing, and courts interpreting it should be sensitive to the reasonable practices that have and will evolve among parties seeking to add to the technological and creative wealth of America.

Among the rights retained by the licensee electing under new Section 365(n)(1)(B) is the right to any embodiment of the intellectual property to which the parties' contracts entitle the licensee. For instance, the parties might have agreed that the licensor would prepare a prototype incorporating the

licensed intellectual property. If such a prototype was prepared prior to the filing of the petition for relief, but had not been delivered to the licensee at that time, then the licensee can compel the delivery of the prototype in accordance with the terms of the rejected license. Other examples of embodiments include genetic material needed to produce certain biotechnological products and computer program source codes. There are many other possible examples of embodiments, but critical to any right of the licensee to obtain such embodiments under this bill is the prepetition agreement of the parties that the licensee have access to such material and the physical existence of such material on the day of the bankruptcy filing.

2. New paragraph (n)(2) of subsection 365(n)

Section 365(n)(2) modifies the rights that a retaining licensee would ordinarily have as the nondebtor party to a contract rejected under section 365. So long as the trustee and its successors in interest allow the licensee to exercise the retention rights set forth in section 365, the licensee

(1) is to make all royalty payments due under the rejected license and any available extension which the licensee elects to exercise and

(2) waives any right to set off damages which it incurred as a result of the trustee's rejection and any claim which it might otherwise be allowed under Section 503(b) of title 11 arising from its performance of the rejected contract.

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This represents a careful compromise between the needs of the debtor and the licensee. The licensee requires retention of its rights, even exclusive rights. No longer can the debtor expect to sell these rights through rejection. The debtor's ability to reorganize may depend upon preservation of the royalty payments called for under the contract, free of offset or administrative claims which could similarly defeat the right to royalty payments. The bill accomplishes this, but leaves unaffected the licensee's rights under Section 365(g), so that a general claim for damages, if any, from rejection can be asserted by the licensee.

3. New paragraphs (n)(3) and (n)(4) of subsection 365(n)

Prior to rejection by the debtor licensor but upon nonperformance by the trustee ((n)(4)), as well as upon rejection by the debtor licensor combined with the licensee's election to retain rights in intellectual property ((n)(3)), the trustee, upon written request by the licensee, as provided in the parties' agreements, shall turn over to the licensee intellectual property held by the trustee and shall not interfere with the licensee's contractual rights to use the intellectual property or to obtain it from a third party. The intellectual property referred to is only that which is in existance at the time of petition filing and not anything which first comes into being post-petition. New paragraphs (n)(3) and (n)(4) do not compel future affirmative performance by the trustee, as distinguished from providing the licensee with access to the existing intellectual property, including the delivery or turnover of any existing items specifically required by the contract, and not interfering with the licensee's rights thereto. It is contemplated that the trustee's undertaking will be

essentially ministerial. Reference to noninterference by the trustee is not intended to imply that the rights of the licensee enjoy any protection from the trustee's avoiding powers under Sections 544 to 549 of the Code.

VII. AGENCY VIEWS

GENERAL COUNSEL OF THE
UNITED STATES DEPARTMENT OF COMMERCE,
Washington, DC.
Hon. JOSEPH R. BIDEN, Jr.,
Chairman, Committee on the Judiciary,
U.S. Senate, Washington, DC.

DEAR MR. CHAIRMAN: Thank you for requesting our views on S. 1626, a bill to keep secure the rights of intellectual property licensors and licensees which come under the protection of the bankruptcy code. The Administration supports this bill and urges its speedy enactment.

S. 1626 would amend title 11 of the United States Code by defining intellectual property and mask works and by preserving the rights of intellectual property licensees when a trustee in bankruptcy rejects an executory contract under which the debtor is the licensor. If the trustee rejects such a contract, the licensee may elect either to treat the contract as terminated by the rejection, if the rejection amounts to a material beach, or may elect to retain certain rights under the contract. The licensee would not be able to demand specific performance of affirmative obligations under the contract except certain obligations necessary it implement

the license agreement. A licensee who elects to retain its rights would be required to make all payments with respect to such rights under the contract and would be deemed to waive any right of setoff it may have with respect to such contract and any claim allowable under § 503(b) of title 11 arising from the performance of the contract.

We believe that S. 1626 fairly addresses an important need. Several recent cases have interpreted intellectual property license agreements as executory contracts, permitting the trustee to reject the contract and terminate the license. In Lubrizol Enterprises, Inc. v. Richmond Metal Finishers, Inc., 226 USPQ 961 (4th Cir. 1985), the court held that a technology licensing agreement was an executive contract under 11 U.S.C. § 365(a), citing the 'unperformed, continuing core obligations of notice and forbearance' on the part of the licensor and the 'unperformed and continuing duty of accounting for and paying royalties for the life of the agreement' on the part of the licensee. Id. at 962.

The obligations of forbearance and payment are the essence of a license arrangement, and the duties of notice and accounting are found in many if not most license arrangements. The holding of the court in Lubrizol therefore makes it virtually impossible to craft a business arrangement that, in jurisdictions following the rationale of Lubrizol, would survive a petition in bankruptcy if the trustee chose to reject the agreement.

We believe this approach places too great a burden on the ability of intellectual property owners to negotiate satisfactory license arrangements. While rejecting an

executory contract would ordinarily preclude the licensee from demanding specific performance, the holding in Lubrizol would treat an intellectual property license—that is, the covenant not to sue for infringement—as an unperformed continuing duty of forbearance for which specific performance could not be demanded if the contract were rejected. Under this approach, a substantial investment by a licensee would be jeopardized if the licensor petitioned in bankruptcy.

This risk will make licensing less attractive to investors, who may require licensors to demonstrate financial stability, and limit its availability as a means to secure development and commercialization of new technology. This will exacerbate the plight of independent inventors, small businesses, and entrepreneurs in high risk areas, who are often without adequate resources and for whom the availability of risk capital is already a major problem. Even for established enterprises, the financial stability of the licensing partner may introduce unacceptable levels of risk and preclude significant investment in technology that must be acquired by license.

We believe the approach of S. 1626 offers a better solution. The trustee would remain free to reject the contract, including specific performance of most aspects of the contract, but the licensee would remain able to secure performance of negative covenants, such as a covenant not to sue or, in the case of an exclusive license, a covenant not to license others to the technology. This approach would add important and needed certainty to licensing transactions and restore the state of the law to that which was understood to exist before Lubrizol.

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Among the rights to specific performance that would be preserved under the approach of S. 1626, in addition to the enforcement of negative covenants relating to a license, the bill would also permit the licensee to demand that the trustee provide any intellectual property, including an embodiment of the intellectual property, held by the trustee, to the extent provided in the license agreement or an agreement supplementary to it. Although 'embodiment' is not defined, we assume the term arises from the copyright law, which provides in section 101 of title 17, United States Code, that a work is 'fixed in a tangible medium of expression when its embodiment in a copy or phonorecord . . . is sufficiently permanent or stable to permit it to be perceived, reproduced, or otherwise communicated for a period of more than transitory duration.' Where the licensed intellectual property is not a work of authorship, we assume the term 'embodiment' would be interpreted in a similar sense of enablement in a manner reasonable in the circumstances and would not necessarily include all physical manifestations of the intellectual property. For example, an embodiment of a licensed process might be interpreted to include technical data sufficient to enable the licensee to operate the process, but not a manufacturing facility using (or embodying) the process; and an embodiment of a licensed invention might be interpreted to include a sample of the invention, but not all inventory.

In this regard, it would be useful for the term 'embodiment' to be interpreted broadly enough to include access to tangible materials required under the license and without which the licensee would be prevented from exercising the license. In biotechnology, for example, a

sample or cell culture may be necessary to enable a person to practice an invention. In such circumstances, if the license provides for delivery of or access to a sample or culture, we believe it would be reasonable to require the trustee either to provide the relevant materials or to permit access to them through another source. This construction should not unduly prejudice the licensor or other creditors and would materially assist certain licensees.

Finally, we believe it would be useful to clarify that termination of an executory contract does not excuse the licensee from certain continuing duties. Since the Lubrizol court has interpreted a duty of forbearance as an unperformed act, we are concerned that a licensee who elects to treat the contract as terminated may believe itself relieved of such continuing obligations as nondisclosure and protection of trade secret information. We believe it would be useful for the legislative history to reflect that a licensor who elects to treat a rejected contract as terminated is not relieved of such continuing obligations as confidentiality and protection of trade secrets. Without this clarification, a trustee may fear that rejecting an executory contract involving a trade secret would jeopardize the trade secret.

We appreciate the opportunity to comment on this bill and urge its speedy enactment.

Sincerely,
ROBERT H. BRUMLEY,
General Counsel.

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VIII. COST ESTIMATE

In accordance with paragraph 11(a), Rule XXVI, of the Standing Rules of the Senate, the committee offers the Report of the Congressional Budget Office:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, August 30, 1988.
Hon. JOSEPH R. BIDEN, Jr.,
Chairman, Committee on the Judiciary,
U.S. Senate, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office has reviewed S. 1626, the Intellectual Property Bankruptcy Protection Act of 1988, as ordered reported by the Senate Committee on the Judiciary, August 10, 1988.

We expect that enactment of the bill would not result in any additional cost to the federal government or to state or local governments. S. 1626 would keep secure the rights of intellectual property licensors and licensees which come under the protection of chapter 11 of the Bankruptcy Code. Specifically, the bill would permit a licensee of intellectual property to elect to use that property, after a trustee rejects the license agreement, to the extent that the use existed immediately prior to the bankruptcy case.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Douglas Criscitello, who can be reached on 226-2850.

Sincerely,
C.G. NUCKOLS
(For James L. Blum, Acting Director.)

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IX. REGULATORY IMPACT STATEMENT

Pursuant to paragraph 11(b), rule XXVI, of the Standing Rules of the Senate, the committee, after due consideration, concludes that the Act will not have direct regulatory impact.

(Note: 1. PORTIONS OF THE SENATE, HOUSE AND CONFERENCE REPORTS, WHICH ARE DUPLICATIVE OR ARE DEEMED TO BE UNNECESSARY TO THE INTERPRETATION OF THE LAWS, ARE OMITTED. OMITTED MATERIAL IS INDICATED BY FIVE ASTERISKS: * * * * *.

2. TO RETRIEVE REPORTS ON A PUBLIC LAW, RUN A TOPIC FIELD SEARCH USING THE PUBLIC LAW NUMBER, e.g., TO(99-495))

S. REP. 100-505, S. Rep. No. 505, 100TH Cong., 2ND Sess. 1988, 1988 U.S.C.C.A.N. 3200, 1988 WL 169875 (Leg. Hist.)